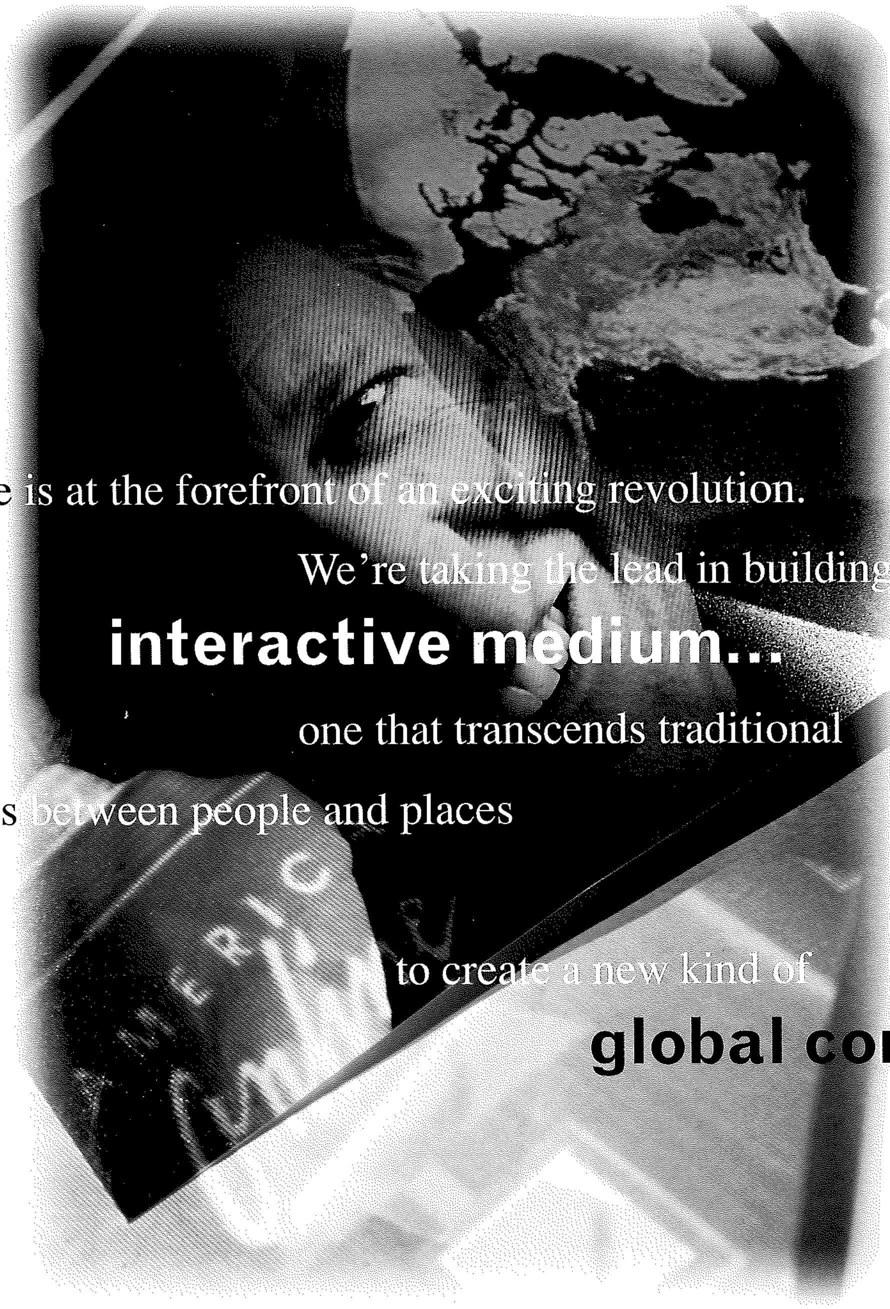
America Online 1995 Annual Report



America Online is at the forefront of an exciting revolution.

We're taking the lead in building a new,

interactive medium...

one that transcends traditional

boundaries between people and places

to create a new kind of

global community.

Corporate Profile

Founded in 1985, America Online, Inc., (NASDAQ symbol: AMER), is the global leader in the market for interactive services. AOL offers its more than 3.5 million members a wide variety of services via personal computer and other intelligent devices. These include electronic mail, conferencing, software, computing support, interactive magazines and newspapers, online classes, as well as easy and affordable access to the Internet. The company has formed dozens of strategic alliances to expand the content and marketing of its services, including alliances with Time Warner, ABC, Knight-Ridder, Tribune, Hachette, IBM and American Express. Headquartered in Vienna, Virginia, AOL employs more than 2500 people located in 16 cities across the United States. Through its joint venture with Bertelsmann AG, one of the world's largest media companies, AOL plans to extend its global presence to Europe in 1995.

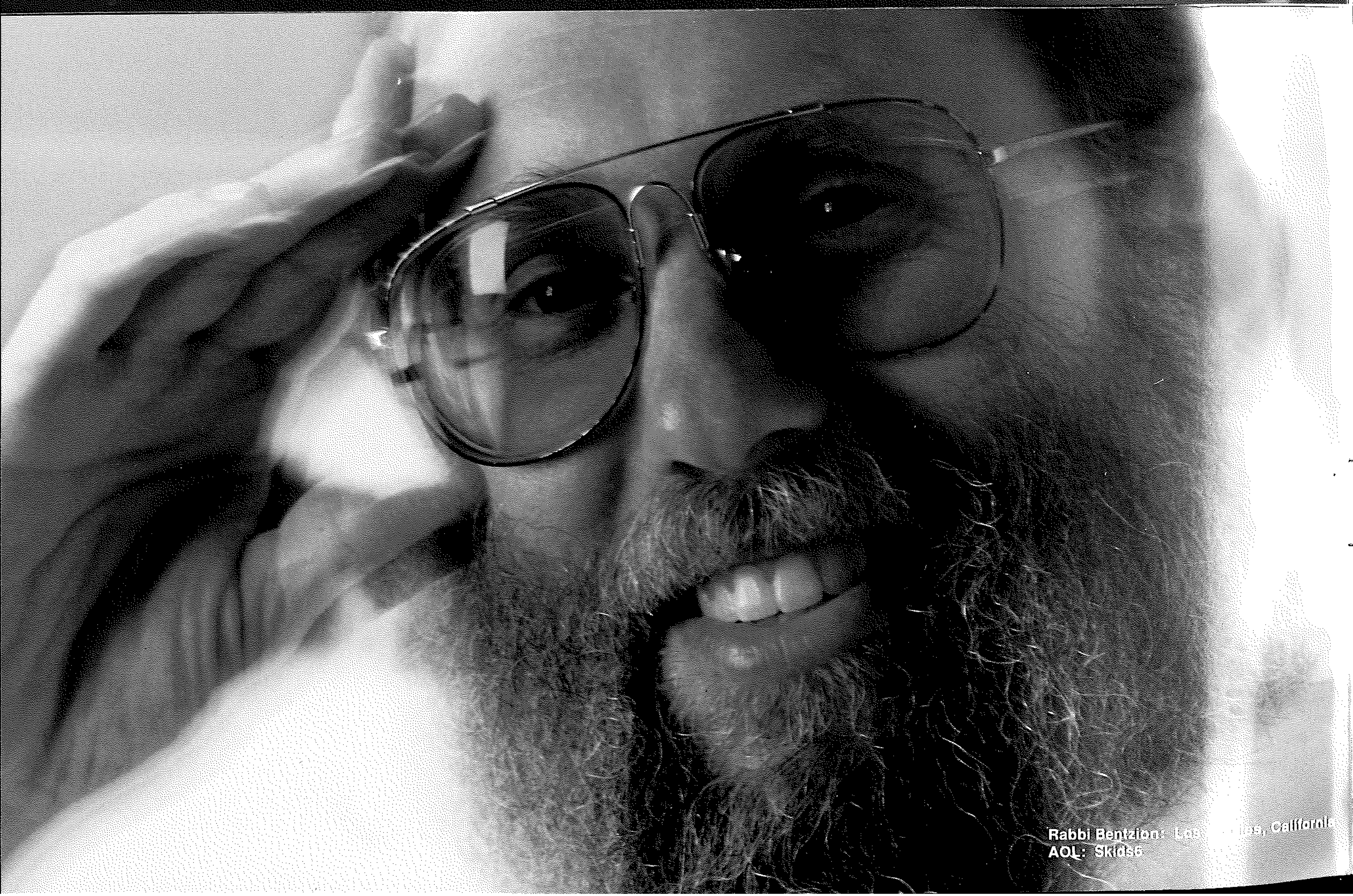
Kate: Crystal City, Virginia
AOL: Mitla

Brian: Laguna Beach, California
AOL: BKim 107199

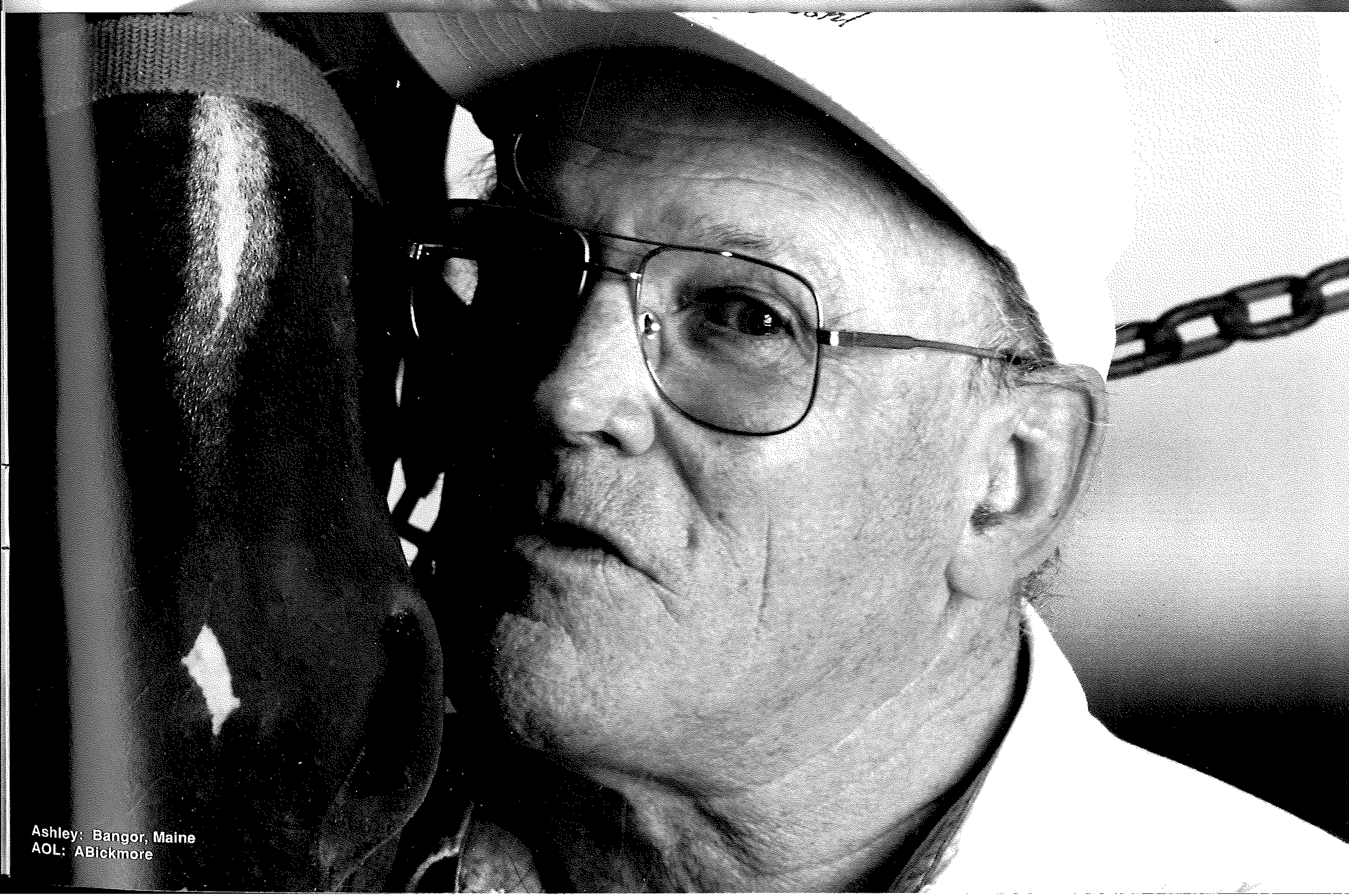
Terri: Mt. Sterling, Kentu
AOL: Battin999

A sense of **community** *... it seldom results from one universal or common element. Communities are more typically derived from special, segmented interests — a neighborhood, a hobby or a strong belief. This interactive medium is unique in that it not only brings to the individual the opportunity to access a vast array of* **content** *spanning virtually all facets of the human experience, but* **communications capabilities** *which bring people together who share common interests and beliefs.*

We are focused on making sure that every individual in our community of more than 3.5 million feels a certain **"connection"** *— a place on AOL that he or she calls home. We want to empower our members to make AOL a more personal service — one that uniquely appeals to the needs and interests of an ever-more diverse member base. We've always known that this has been key to the success of AOL, and we will invest heavily to maintain this critical competitive advantage.*



Rabbi Bentzion: Los Angeles, California
AOL: Skids6



Ashley: Bangor, Maine
AOL: ABickmore

Highl

Significant Member Growth

AOL surpassed many significant milestones before reaching the #1 position in the interactive services market. In August 1994, the Company announced that it had surpassed the 1 million member mark; by the close of the fiscal year the number of members had tripled to 3 million. In just two years, the number of **AOL** members has grown more than ten-fold.

Strategic Acquisitions

AOL acquired the talents and award-winning technologies of several companies including **BookLink** Technologies, **NaviSoft**, **WAIS**, **Medior**, **Redgate**, **ANS** and **GNN**. The combined capabilities represented by these companies have helped to strengthen **AOL's** lead in the converging worlds of online services, the Internet and multimedia.

Stock Splits

In keeping with the Company's long-term strategy of broadening the stockholder base and increasing the liquidity of the Company's shares, AOL's stock split twice. First in November 1994, and then again in April 1995.

Internet Lead Strengthened

AOL launched an award-winning "browser" in the Spring, giving its members access to the vast resources of the World Wide Web. In addition, the Company announced plans for the launch of an Internet-only brand, scheduled for Fall 1995.

Network Expansion

With the acquisition of ANS in November, the Company introduced "AOLnet" giving its members increased capacity and the ability to access AOL at speeds of 14.4 and 28.8 kbps at no extra charge. Aggressive buildout continues as more cities are added each month.

ights

International Expansion

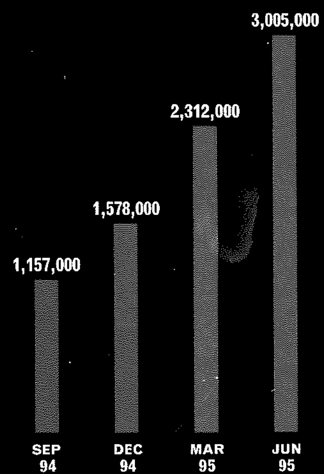
In February, AOL formed a joint venture with Bertelsmann AG, a worldwide leader in the publishing and marketing of books, periodicals, magazines and music, in order to expand AOL's presence overseas. The first European service is expected to launch in Germany by late 1995, and soon thereafter in France and the UK. By linking localized content offerings with an international set of services and members, this new alliance will help to expand the global community of AOL.

Engaging Presentation

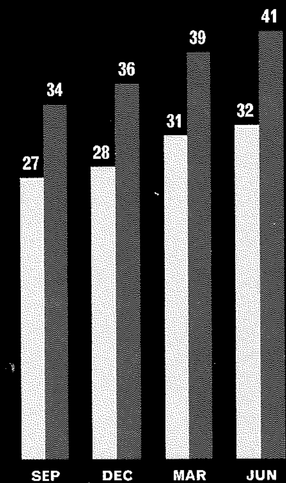
To link online content, multimedia and the Internet together in a more engaging and unified way, AOL introduced a new multimedia interface in the Fall, and acquired Medior, a leading multimedia developer in the Spring. Together these moves give AOL the ability to leverage the rich, engaging appeal of multimedia with the real-time and community attributes of the online environment.

Content Differentiation

The AOL Greenhouse was introduced to give entrepreneurs the opportunity to help build creative, compelling new content and leverage AOL as a launchpad to build cross-media franchises. The response has been overwhelmingly positive as services ranging from Hecklers Online to the eGG have been introduced and met with wide acclaim in the market.

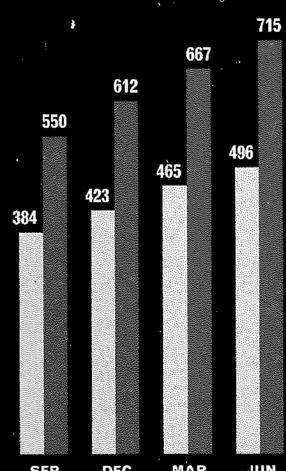


Subscribers at year end
Number of Subscribers



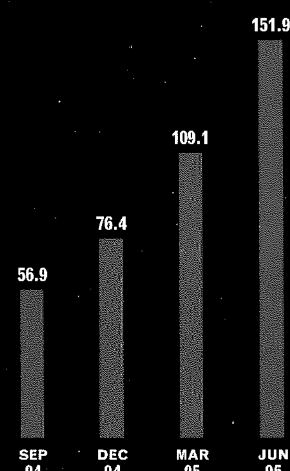
Average Customer Life
Months Spent on Service

FY 94 FY 95



Lifetime Revenues Per Subscriber
Amounts in Dollars

FY 94 FY 95



Fiscal 1995 Quarterly Revenues
Amounts in Millions of Dollars

Club KidSoft Computing/Print & Broadcast Worldwide ABC News Debates and Discussions

Dear Shareholder:

America Online is at the forefront of an exciting revolution. We're taking the lead in building a new, interactive medium which holds the potential to change the way people get information, communicate with one another, buy products and learn new things. We are encouraged by the momentum we are seeing in the market, and we believe we are well-positioned to prosper. Our aim is to build a mass market for interactive services — and to do so, we must reach out to the 93% of households who don't currently subscribe to any online service.

We've grown ten-fold in just two years to become #1 in our market, and we are now in a position to become the first interactive services company with annualized revenues of $1 billion.

We are encouraged by the momentum we are seeing in the market, and we believe we are well-positioned to prosper. We've grown ten-fold in just two years to become number one in our market, and we are now in a position to become the first interactive services company with annualized revenues of $1 billion.

Our accomplishments of this past year have been remarkable with significant achievements in member and revenue growth, development of key strategic alliances, creation of new and compelling content and technology advancements. But more importantly, fiscal 1995 was a pivotal year for America Online and a time of vast change in the market for interactive services. The AOL community expanded to include millions of new members, thousands of new employees, hundreds of new alliances, dozens of joint ventures and seven new companies that are doing business under the AOL banner today. And although fiscal 1995 was the year in which we seized the #1 position in the worldwide market for interactive services, it was also a year in which we were driven more by what the future may bring than by the accomplishments of the past; we have been totally and passionately focused on making America Online the service of choice for millions of consumers in an ever-more crowded market.

Unprecedented Results

Unprecedented member growth continued through the fiscal year, tripling to 3 million by year end, was indicative of the continued strong momentum and positive word of mouth for AOL. We significantly increased the level of investment in direct marketing, OEM bundling agreements and media partnerships throughout the year as our growing momentum in the market contributed to gratifying results in these programs.

Member satisfaction — as measured by average use and retention — reached an all time high. Average use per member climbed 30% to exceed 6.5 hours per month. Average member life rose to 41 months in the fourth quarter, contributing to an average lifetime revenue of $715, up considerably from 32 months and less than $500 respectively, in the same quarter a year ago.

Strong member growth helped propel revenue growth 240% to $394.3 million, up from $115.7 million in fiscal 1994. Other revenues continued to climb, driven mostly by revenues from the Company's recently acquired-strategic businesses. For fiscal 1995 in total, our net income before charges and expenses in connection with our acquisition of seven companies during the year was nearly $20 million, as compared with $2.6 million in fiscal 1994. Those charges and expenses — totaling $52.5 million — resulted in a final reported loss for the year of $33.6 million, or $0.99 per share.

The New AOL

Our strategy has always been to provide the "best of breed" service that provides consumers with an easy-to-use and engaging interface, a vast array of compelling content, simple and affordable pricing, and simple, fast and reliable connection and support. Throughout fiscal 1995 we made significant advances in each of these areas, largely through newly formed alliances, strategic acquisitions, joint ventures, and the expansion of our operations in new areas.

Leveraging the Internet Phenomenon

We believe that some of the best work in the market is being done by small companies focusing exclusively on innovating in a specific area of interactive services. Nowhere is this more evident than in the Internet arena. As we expanded

our offerings to include the full suite of Internet applications, we identified and acquired the best technology and talent to rapidly accelerate our lead in this segment of the market. In the Fall of 1994, we announced the acquisition of BookLink Technologies and NaviSoft, two companies who together brought to America Online award-winning technology to strengthen our capabilities in helping consumers access and create content on the World Wide Web. With the introduction of our easy-to-use Internet "browser," we believe we have introduced a whole new class of consumers to the Web.

Also on the Internet front, we acquired Global Network Navigator (GNN), one of the most highly trafficked sites on the Web. GNN has been heralded as a leader in providing easy and intuitive navigation for consumers who want to explore the many and varied resources of the Web. It will play a critical role in providing content and "context" for AOL's new standalone Internet brand, expected to launch in the Fall of 1995. Two other acquisitions, WAIS and the WebCrawler technology, helped to strengthen the Company's Internet capabilities. WAIS, widely recognized as the leading publishing system for the Internet, enables us to offer our partners a complete solution to World Wide Web access, from production of a Home Page to full administration of the Web site once it's up and running. WebCrawler, the first full-text search service available on the Internet, strengthens both the AOL service and our Internet brand offerings.

Enhancing the AOL Experience

Early in the fiscal year we introduced a new, more engaging interface featuring an expanded array of new "channels" or content areas. Our tapestry of strategic alliances grew to include new content providers such as American Express, ABC, Reuters, Shoppers Express, Business Week, Fidelity, Vanguard, the National Education Association and many, many more. These alliances, along with hundreds of other new services that were added, strengthened the breadth and depth of AOL's content to better meet the needs of a growing and diverse electronic community.

We also participated in numerous joint ventures to build and create unique content to serve the entire AOL community. These ventures have helped to make AOL a magnet for the best creative and entrepreneurial talent in the market today, and they're designed to build new brands for the next decade. The AOL Greenhouse was introduced to give entrepreneurs the opportunity to help build creative, compelling new content, and leverage AOL as a launchpad for cross-media franchises. The response has been overwhelmingly positive as services ranging from Afro-centric to the golf enthusiast met with wide acclaim in the market.

While content plays a critical role in helping to meet the needs of our community, another important ingredient is the "context" in which content is presented. Our focus is on building an integrated strategy to link online content, multimedia and the Internet together in a more engaging and unified way. The introduction of our new multimedia interface last Fall was a first step in this direction. To further this strategy, in the Spring we acquired Medior, a company recognized as the leading developer of interactive media properties. Using the creative talents and expertise of Medior we are better positioned to leverage the rich, engaging appeal of multimedia with the real-time and community attributes of the online environment.

We're also focused on improving the navigation and personalization of our services. Several new features ranging from personal publishing capabilities to enhanced parental controls are helping our members create and control their own, individual online experience. We recently introduced "My Home Page," allowing members to quickly and easily create their own personal home page with text, photos and graphics on the Web that can be accessed by friends and associates both inside and outside of the AOL community. In addition, we launched "My Place," providing each AOL member with ample space to publish on the Web. Personalization of our services is an area of growing importance as advanced technical capabilities merge with an ever-more diverse member base to redefine AOL on a personal level according to the needs and interests of the individual consumer.

As we expanded our Internet offerings to include the full suite of applications, we identified and acquired the best technology and talent to rapidly accelerate our lead in this important segment of the market.

Fast and Reliable Connection and Support

One of our highest priorities entering fiscal 1995 was to build and strengthen network access for a rapidly growing member population. The surge in our member base combined with the expanded delivery of Web and multimedia capabilities on AOL represented a new challenge for us on the network front. To respond to this, we launched a strat-

egy that would allow us to provide increased capacity and higher speed access for our members, while at the same time lowering our cost structure. With the acquisition of ANS, the company that created the backbone of the global Internet and the operator of one of the nation's largest and fastest data networks, we introduced "AOLnet," giving our members increased capacity and the ability to access the service at speeds of 14.4 and 28.8 kbps at no extra charge. We spent the last half of the fiscal year building out AOLnet to 116 cities and approximately 20,000 modems. Buildout will continue as we strive to stay ahead of demand and maintain our competitive lead in the online services industry.

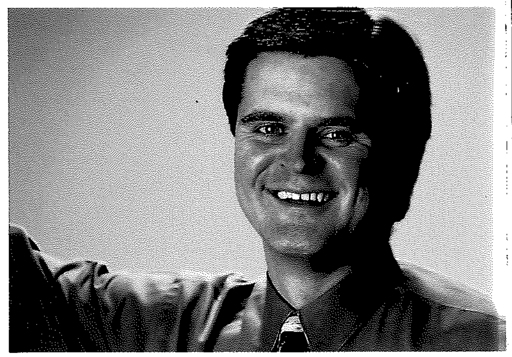
Another area of importance for us is member service. This past year we made significant investments and vastly expanded our operations to improve the level, quality and timeliness of our support. We now have more than 1250 people in support, and we've added two new customer support centers — one in Tucson and one in Jacksonville. In addition, we recently unified the billing, sales and technical service into a single group called Member Services to make sure that we're providing our members with a single point of contact. We will continue to expand our customer support operations to ensure that supply stays ahead of demand.

Global Expansion

We've always believed that there was a tremendous opportunity for America Online to build a global presence. Interactive services in Europe and in Japan have traditionally been limited in scope and lacking in graphical appeal for consumers. That gives AOL a unique opportunity to leverage its strengths in a fairly untapped market. However, we were committed to first building critical mass in the U.S. before we felt it was appropriate to extend our efforts overseas. In the Spring, as we surpassed the 2 million mark, it became clear that the time had come for us to leverage this global market opportunity. To begin to do so, we formed a joint venture with Bertelsmann AG, a worldwide leader in book and magazine publishing, and music and television and record/book club marketing. Bertelsmann brings to the joint venture access to their publishing content and book and music club member base (more than 30 million people worldwide), while America Online brings its leadership in developing, managing and operating interactive services. We expect to launch the first European services in Germany, France and the U.K. in fiscal 1996. These services will link local content offerings with an international set of services and members, helping to expand the global community of AOL. We plan to introduce similar services in Japan in the future.

Leading the Way

When we started America Online a decade ago, we dreamed of the day when tens of millions of people would be connected to online services, how those services could change the way people obtain information, communicate with other people, shop for products and services, and learn new things. In those early years, our Chairman, Jim Kimsey, took the lead in translating those possibilities into a viable business. Jim was instrumental in raising capital, assembling the management team, and establishing the core alliances. More recently, even as his active involvement in the business diminished, Jim has remained an important advisor to me. Now, on the 10th anniversary of the founding of the company, Jim has decided to step down as Chairman, so he can apply his talents and resources to the advancement of humanitarian efforts and diplomatic causes worldwide. We are grateful for the many contributions he has made over the years, and I am particularly pleased that he has agreed to continue on as a Director and will continue to be available to me as a source of counsel and advice.



Stephen M. Case, President and CEO

For us, however, the challenge remains the same — we will continue to focus on strengthening our lead in the market, especially in light of new, formidable competition. We plan to do so with the same formula for success that has made us what we are today — the unique combination of content, context, community, connectivity and low cost. We believe we are well positioned to help drive this new medium from a niche market to a mass market with broad consumer appeal. The achievements of the past year have helped AOL to secure a leadership role as we look toward the 21st century.

Sincerely,

Steve Case
President & CEO

Medior

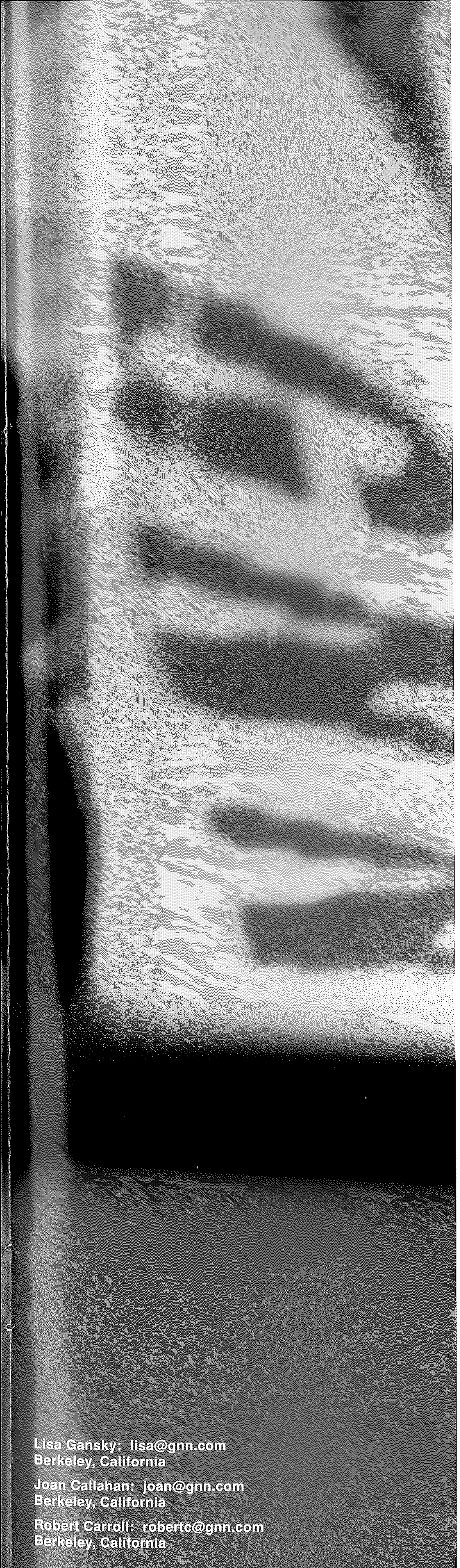
In the Spring, AOL acquired Medior, a company widely recognized as the leading developer of interactive media properties.

America Online and Medior share a vision for interactive publishing that marries the rich, engaging appeal of multimedia with the real-time and community attributes of the online environment. Medior is expected to play a key role in helping to continue to enhance and transform America Online's "look and feel" through the seamless integration of text, photos, graphics and sound.

GNN

In June, AOL acquired Global Network Navigator (GNN). GNN has been widely heralded as a leader in providing easy and intuitive navigation for consumers who want to explore the many and varied resources of the Web. GNN is expected to play a critical role in providing content and "context" for AOL's new standalone Internet brand, scheduled to launch in the Fall of 1995. GNN will also be working with publishers to offer members a wide range of a la carte services using the open Internet model.

Sports/Local Coverage Going Places What's Hot This Month Chicago Tribune America



Context

Our focus is to improve the "context" in which content is presented — doing a better job of linking AOL, the Internet and multimedia together in a more engaging and integrated way.

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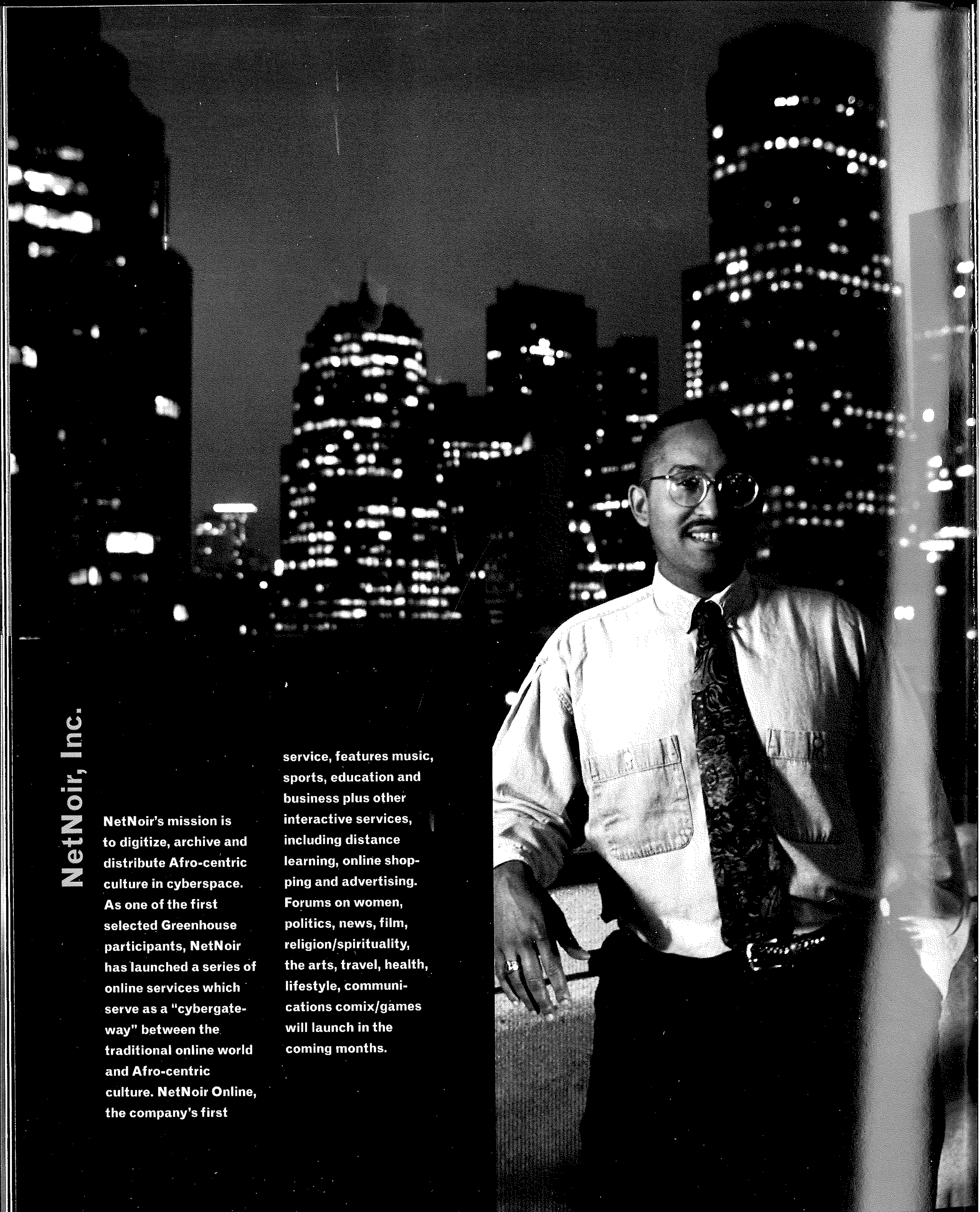
The introduction of our Internet browser in the Spring provided capabilities which allowed us to leverage the vast content of the Internet to enhance the breadth of our own content areas. But rather than simply providing a separate connection to the Web — as most other browsers provided by online services do — we focused on using our browser to make the Web useful and intuitive. Specifically, we integrated Web access within AOL and categorized services based on areas of consumer interest. This integrated approach vastly improves the context in which a consumer can find relevant services, and also makes the Web feel like part of AOL, rather than like a foreign land.

Each of AOL's 14 service channels now guides members to relevant content by highlighting a selection of the most popular Web sites, categorized by topic of interest. The best sports-related content, for example, is logically grouped together under Sports, irrespective of whether the content is stored on AOL itself or on Web servers. This integrated approach also enables our members to continue to use the full suite of AOL features while exploring the Internet. Members are now able to have Web Pages and AOL screens open simultaneously — allowing them to chat, send E-mail and Instant Messages, and download while at the same time they explore the Web.

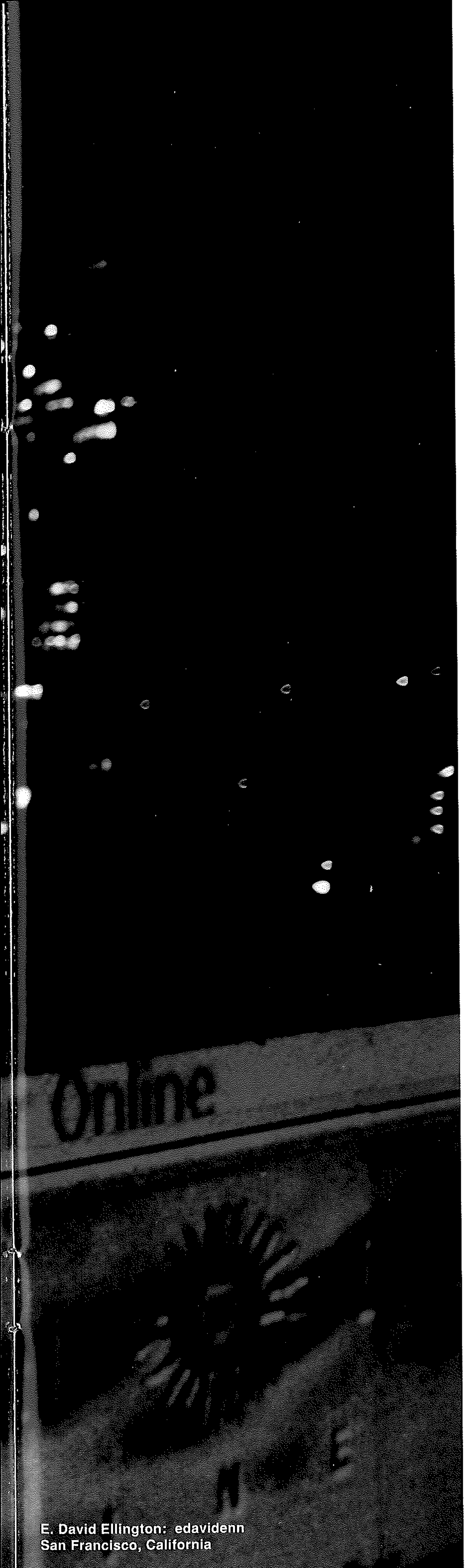
We've also introduced software enhancements to allow our members to personalize the context in which content is presented. Our new Windows software, for instance, includes a Favorite Places personalized navigator, allowing members to "drag and drop" frequently accessed areas of either AOL or the Web into a personal menu. On subsequent visits, members can jump directly to the desired areas, whether it's a message board on AOL or a Web site.

In the Spring we also announced a series of new alliances with leading CD-ROM publishers to deliver companion CD-ROM's for each of our 14 content channels, blending the best of CD-ROM such as engaging video, audio and extensive database capabilities, with the best of online services and the Internet — community, real-time updating of content and interactivity — to create a unique and compelling interactive experience for consumers.



NetNoir, Inc.

NetNoir's mission is to digitize, archive and distribute Afro-centric culture in cyberspace. As one of the first selected Greenhouse participants, NetNoir has launched a series of online services which serve as a "cybergateway" between the traditional online world and Afro-centric culture. NetNoir Online, the company's first service, features music, sports, education and business plus other interactive services, including distance learning, online shopping and advertising. Forums on women, politics, news, film, religion/spirituality, the arts, travel, health, lifestyle, communications comix/games will launch in the coming months.



E. David Ellington: edavidenn
San Francisco, California

Content

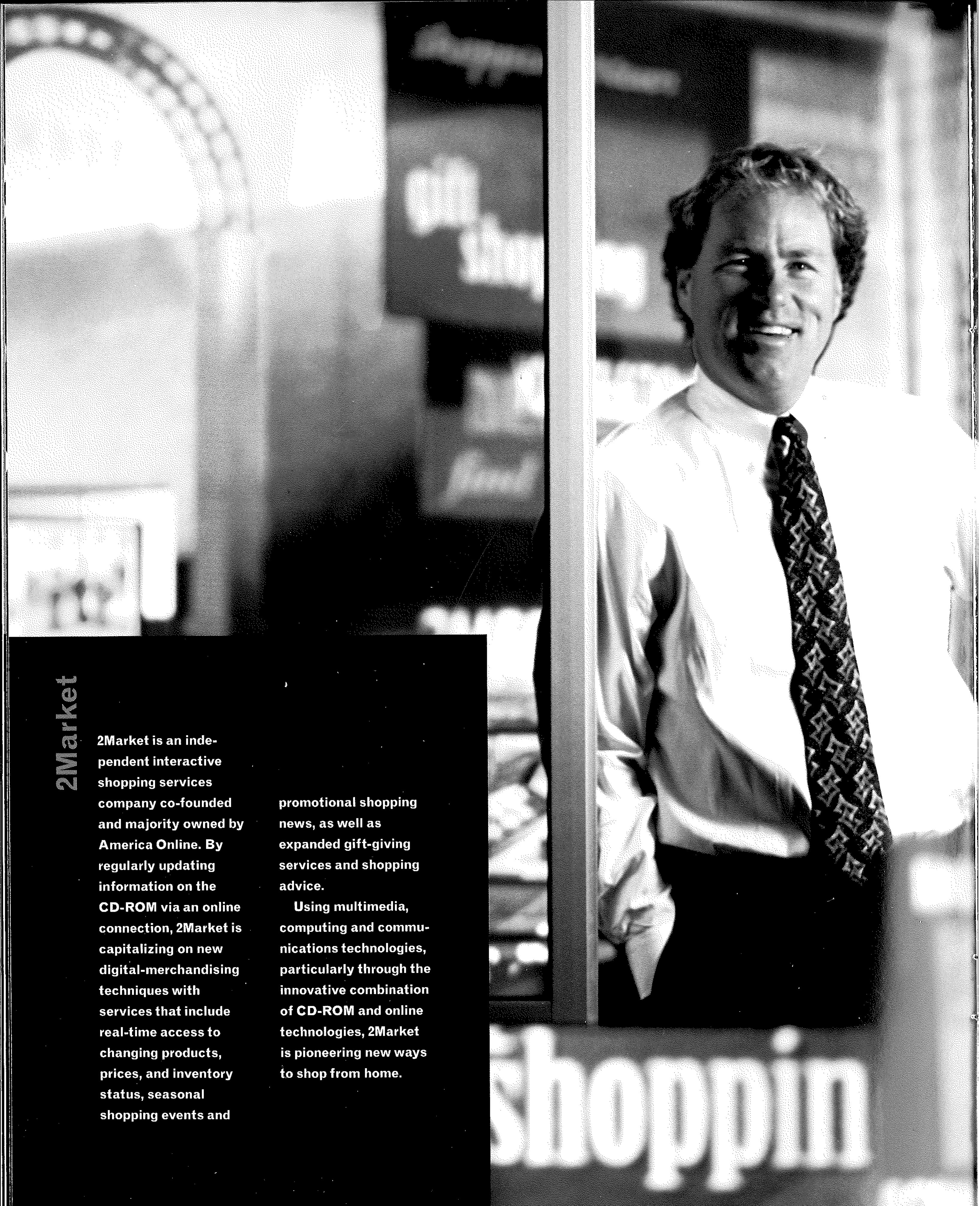
The Company participated in numerous joint ventures to build and create unique content to serve the entire AOL community. These ventures have helped to make AOL a magnet for the best creative and entrepreneurial talent in the market today.

Providing consumers with breadth and depth of content has always been an important component in AOL's formula for success. We've made great strides this past year in adding content that provides differentiation, ranging from special interest to branded content that offers mass market appeal.

Through a series of strategic investments and joint ventures, AOL has become a magnet for the best creative and entrepreneurial talent in the market. Where in the past online services were the last stop in the value chain for traditional media to simply use the medium to repurpose content, today exciting opportunities exist to work with partners to "nest" new brands for the next decade. These investments are designed to provide content differentiation in the short run and business appreciation over the long run as they evolve into valuable cross-media brands and leverage multiple distribution channels.

Early in the fiscal year the Company introduced a new, more engaging interface featuring an expanded array of new "channels" or content areas. Along with these new channels came a growing number of important new strategic alliances that serve to strengthen the breadth and depth of content in each of these areas. Special interest content from the American Diabetes Association to Christianity Today was added, as was content from major media companies including ABC, Business Week and American Express, and many, many more.

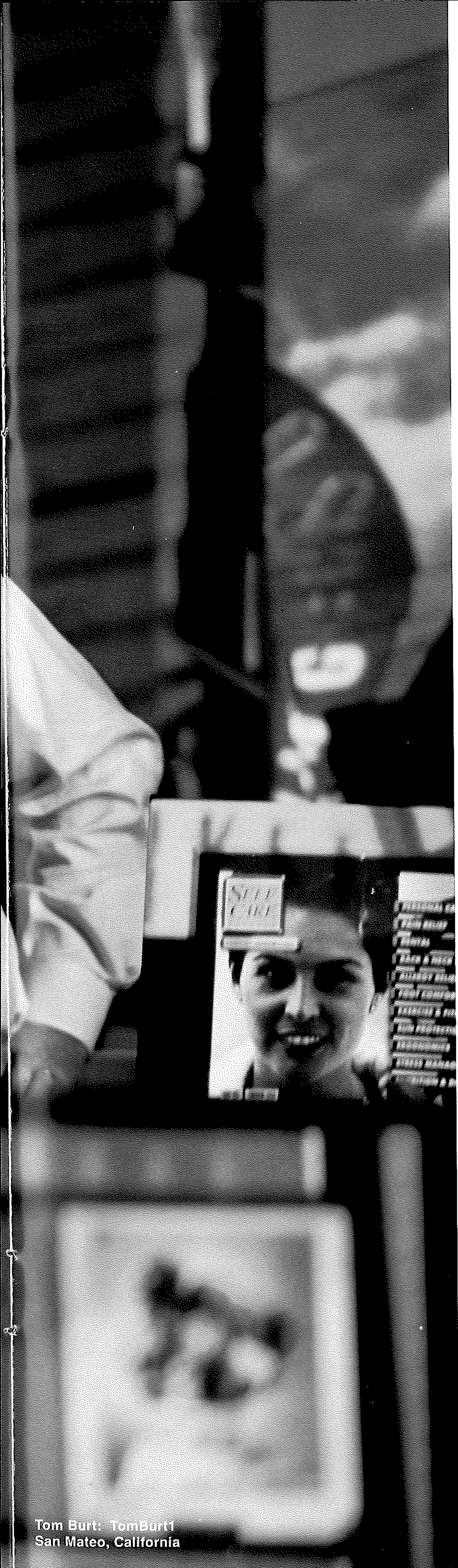
The AOL Greenhouse was introduced in the Fall to give entrepreneurs the opportunity to help build creative, compelling new content and leverage AOL as a launchpad to build cross-media franchises. The response has been overwhelmingly positive, and there are already some Greenhouse "stars" that are starting to make the vision of the Greenhouse program an exciting reality. Motley Fool, for instance, was one of the earliest participants in the Greenhouse program. Motley Fool started out by offering an online investment area that strayed from the button-down environment that usually exists for such subject matter. The unique "point of view" members found in the Motley Fool area quickly resulted in it becoming one of the most popular services on America Online. From there the founders, Tom and David Gardner, took their idea and expanded it to an area focused on entertainment entitled "Follywood." The successful "buzz" surrounding the Motley Fool — and the recognition that they have created a unique subculture on AOL — has resulted in a book and movie deal for the duo. Our hope is that what has been created here is not only a service that helps to differentiate AOL from its competitors, but one that will transcend mediums and be carried into the next decade as the popularity with consumers continues to surge.



2Market

2Market is an independent interactive shopping services company co-founded and majority owned by America Online. By regularly updating information on the CD-ROM via an online connection, 2Market is capitalizing on new digital-merchandising techniques with services that include real-time access to changing products, prices, and inventory status, seasonal shopping events and promotional shopping news, as well as expanded gift-giving services and shopping advice.

Using multimedia, computing and communications technologies, particularly through the innovative combination of CD-ROM and online technologies, 2Market is pioneering new ways to shop from home.



Tom Burt: TomBurt1
San Mateo, California

Commerce

AOL is uniquely positioned to capitalize on its growing base of millions of active members, along with advancements in presentation, automation, personalization and navigation on its service and on the Web, to redefine advertising in this interactive medium.

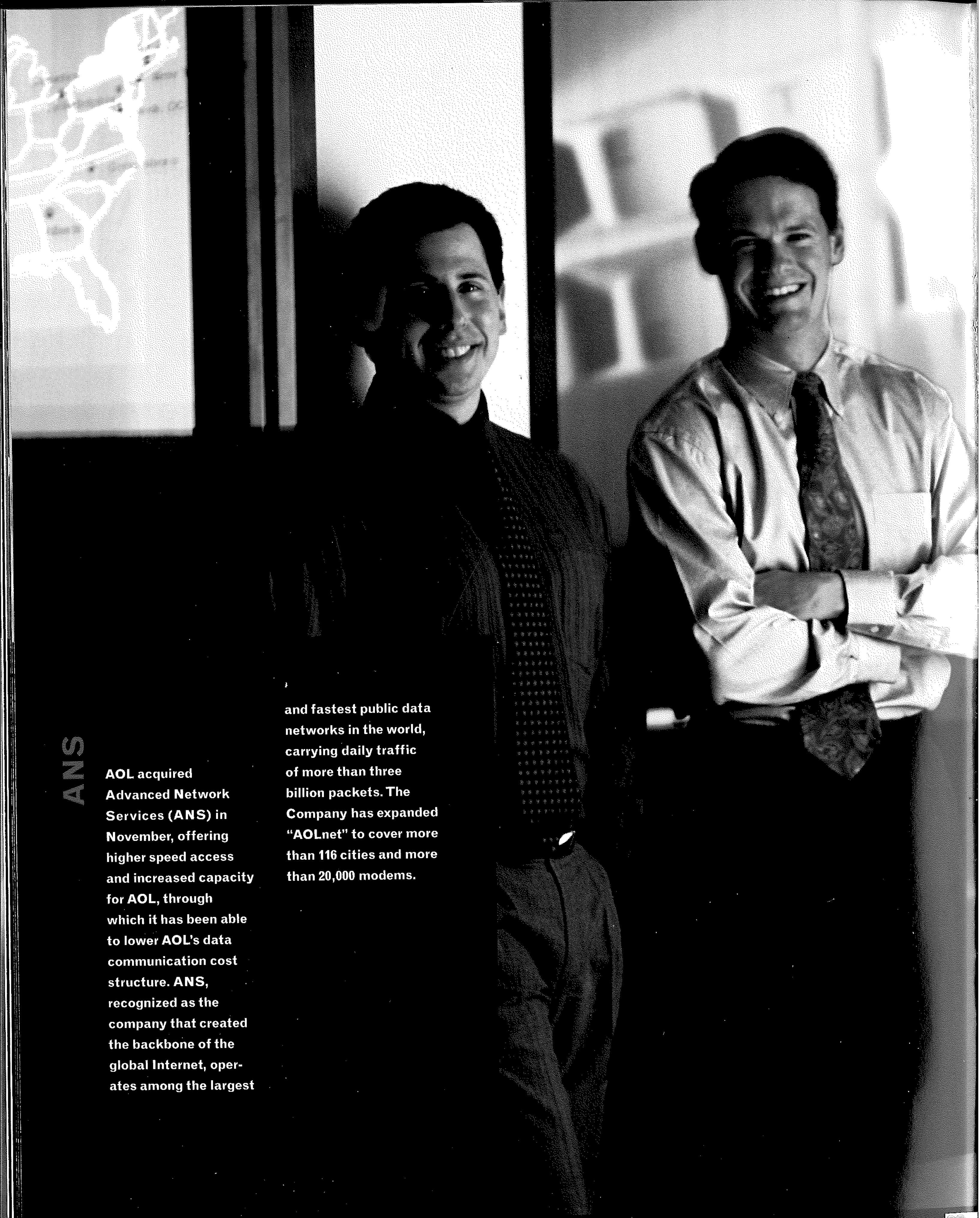
As industries converge in this new medium, a new revolution is taking place which is changing all of that. Now, smart companies are creating different kinds of messages with different points of view for different market segments. They're recognizing that the consumer — armed with informative facts — will actually make smarter buying decisions. Interactive services are personalizing information and communication for consumers, and as such are beginning to change the way consumers learn about and purchase goods and services. In this new interactive medium, advertising is about creating interesting information and putting it in new channels that connect buyers and sellers based on segmented areas of interest. And it's about interaction — buyers talking to sellers or buyers exchanging opinions with other buyers — all geared toward one goal, empowering the consumer to make an informed decision.

AOL is uniquely positioned to capitalize on its growing base of millions of active members, along with advancements in presentation, automation, personalization and navigation on its service and on the Web, to redefine advertising in this interactive medium. This past year, AOL made great strides in providing transactional services for consumers and in introducing new forms of interactive marketing.

Throughout the year we expanded our agreements with content providers, offering them new business opportunities and a chance to bring their products and services onto AOL, the Internet and CD-ROM. In the Fall, we announced the formation of 2Market, a company co-founded with Apple Computer and Medior. 2Market is an interactive personal shopping service for CD-ROM and online, featuring thousands of goods and services from leading catalogs and retailers, as well as a one-step connection to America Online.

AOL also launched the "Marketplace" channel in the Fall. Many merchants and major brand names have enjoyed success on this channel, including Hallmark, Tower Records, 1-800 Flowers, and Hanes. Oldsmobile's own area on AOL not only includes an Oldsmobile showroom but a "Celebrity Circle" auditorium featuring such personalities as Clive Barker and Sandra Bullock. On the Web, AOL maintains a service called "Downtown AOL," populated by an eclectic group of merchants.

We anticipate that new revenue sources from advertising and transactions will help to fuel broader investments in R&D, innovative content and affordable pricing, allowing AOL to maintain its competitive edge. As technology advancements continue, and this medium moves to the masses, we expect interactive marketing to play an important role in helping to meet the needs and interests of our member base.



ANS

AOL acquired Advanced Network Services (ANS) in November, offering higher speed access and increased capacity for AOL, through which it has been able to lower AOL's data communication cost structure. ANS, recognized as the company that created the backbone of the global Internet, operates among the largest and fastest public data networks in the world, carrying daily traffic of more than three billion packets. The Company has expanded "AOLnet" to cover more than 116 cities and more than 20,000 modems.

Jordan Becker: Becker@ans.net
Elmsford, New York

Carl Showalter: Carl@ans.net
Elmsford, New York

Communications

We continue to invest heavily in increasing network capacity and high speed access to AOL to satisfy the increased demand for faster, more reliable communications.

Although AOL's content has expanded significantly to include a vast array of rich and engaging new services, it is the personal, member-to-member interaction which still comprises the vast majority of AOL usage today. Whether exchanging thoughts and opinions in a message board; leading a group of friends, colleagues or potential business associates on a trip through the Web and AOL via our "Road Trip" feature; using e-mail to communicate with friends and family members; or joining in on a real-time conference with a celebrity, millions of consumers every day turn to AOL for personal communications.

We continue to invest heavily in increasing network capacity and high speed access to AOL to satisfy the increased demand for faster, more reliable communications. Through the acquisition of ANS, the company that created the backbone of the global Internet and the operator of one of the nation's largest and fastest data networks, we introduced "AOLnet," giving our members increased capacity and the ability to access the service at speeds of 14.4 and 28.8 kbps at no extra charge. We spent the last half of the fiscal year successfully building out AOLnet to its current level of 116 cities and approximately 20,000 modems, and more cities are being added each month. We also now offer an 800 number access option for connecting to AOL for members who frequently travel or who live in rural areas not presently served with a local access number.

In addition to meeting the communications needs of individuals, we now believe we have acquired the right combination of assets to extend our reach into the corporate market. By leveraging the investments we have made in technology and in the AOLnet network, we believe we are well positioned to meet the growing communications needs of businesses that want fast and reliable network reach combined with a flexible architecture that can grow with them into the 21st century. By providing services to the corporate market, we will also begin building bridges and gaining early experience as the lines between the business and the personal market for interactive services begin to converge.

Selected Consolidated Financial and Other Data

(Amounts in thousands, except per share data)	Year Ended June 30,				
	1995	1994	1993	1992	1991
Statement of Operations Data:					
Online service revenues	**$358,498**	$ 100,993	$ 38,462	$ 26,226	$ 19,515
Other revenues	**35,792**	14,729	13,522	12,527	10,646
Total revenues	**394,290**	115,722	51,984	38,753	30,161
Income (loss) from operations	**(19,294)**	4,608	1,925	3,685	1,341
Income (loss) before extraordinary item	**(33,647)**	2,550	399	2,344	1,100
Net income (loss)[1]	**(33,647)**	2,550	1,532	3,768	1,761
Income (loss) per common share:					
Income (loss) before extraordinary item	**$ (0.99)**	$ 0.07	$ 0.01	$ 0.10	$ 0.06
Net income (loss)	**$ (0.99)**	$ 0.07	$ 0.05	$ 0.17	$ 0.09
Weighted average shares outstanding	**33,986**	34,208	29,286	22,828	19,304
	As of June 30,				
	1995	1994	1993	1992	1991
Balance Sheet Data:					
Working capital (deficiency)	**$ (456)**	$ 47,890	$ 10,498	$ 12,363	$ (966)
Total assets	**406,464**	154,584	39,279	31,144	11,534
Total debt	**21,810**	9,302	2,959	2,672	1,865
Stockholders' equity (deficiency)	**217,944**	98,297	23,785	21,611	(8,623)
Other Data (at fiscal year end):					
Subscribers	**3,005**	903	303	182	131

[1] Net loss in the fiscal year ended June 30, 1995 includes charges of $50.3 million for acquired research and development and $2.2 million for merger expenses. See Note 3 of the Notes to Consolidated Financial Statements.

Management's Discussion and Analysis of Financial Condition and Results of Operations

Overview

The Company has experienced a significant increase in revenues over the past three fiscal years. The higher revenues have been principally produced by increases in the Company's subscriber base resulting from growth of the online services market, the introduction of a Windows version of America Online in the middle of fiscal 1993, which greatly increased the available market for the Company's service, as well as the expansion of its services and content. Additionally, revenues have increased as the average monthly revenue per subscriber has risen steadily during the past three years, primarily as a result of an increase in the average monthly paid hours of use per subscriber.

The Company's online service revenues are generated primarily from subscribers paying a monthly membership fee and hourly charges based on usage in excess of the number of hours of usage provided as part of the monthly fee. Through December 31, 1994 the Company's standard monthly membership fee, which includes five hours of service, was $9.95, with a $3.50 hourly fee for usage in excess of five hours per month. Effective January 1, 1995, the hourly fee for usage in excess of five hours per month decreased from $3.50 to $2.95, while the monthly membership fee remained unchanged at $9.95.

The Company's other revenues are generated primarily from providing new media and interactive marketing services, data network services, and multimedia and CD-ROM production services. Additionally, the Company generates revenues related to online transactions and advertising, as well as development and licensing fees.

In fiscal 1995 the Company acquired Redgate Communications Corporation ("RCC"), NaviSoft, Inc. ("NaviSoft"), BookLink Technologies, Inc. ("BookLink"), Advanced Network & Services, Inc. ("ANS"), Wide Area Information Servers, Inc. ("WAIS"), Medior, Inc. ("Medior") and Global Network Navigator, Inc. Additionally, in August 1995, the Company entered into an agreement to acquire Ubique, Ltd. ("Ubique"). For additional information relating to these acquisitions, refer to Notes 3 and 13 of the Notes to Consolidated Financial Statements.

The online services market is highly competitive. The Company believes that existing competitors, which include, among others, CompuServe, Prodigy and the Microsoft Network, are likely to enhance their service offerings. In addition, new competitors have announced plans to enter the online services market, resulting in greater competition for the Company. The competitive environment could require new pricing programs and increased spending on marketing, content procurement and product development; limit the Company's opportunities to enter into and/or renew agreements with content providers and distribution partners; limit the Company's ability to grow its subscriber base; and result in increased attrition in the Company's subscriber base. Any of the foregoing events could result in an increase in costs as a percentage of revenues, and may have a material adverse effect on the Company's financial condition and operating results.

During September 1995, the Company modified the components of subscriber acquisition costs deferred and will be expensing certain subscriber acquisition costs as incurred, effective July 1, 1995. All costs capitalized before this change will continue to be amortized. The effect of this change for the year ended June 30, 1995 (including the amortization of amounts capitalized as of June 30, 1994) would have been to increase marketing costs by approximately $8 million. This change will have a greater impact on the Company's marketing costs in fiscal 1996, as the Company expects to significantly increase subscriber acquisition activity, including those subscriber acquisition expenditures which the Company will be expensing as incurred.

In addition, effective July 1, 1995 the Company changed the period over which it amortizes subscriber acquisition costs from twelve and eighteen months to twenty-four months. Based on the Company's historical average customer life experience, the change in amortization period is being made to more appropriately match subscriber acquisition costs with associated online service revenues. The effect of this change in accounting estimate for the year ended June 30, 1995 would have been to decrease the amount of the amortization of subscriber acquisition costs by approximately $27 million. While this change will thereby positively impact operating margins, the Company expects that any such positive impact will be partially offset by increased investments in marketing and other business activities during fiscal 1996 and the decision, effective July 1, 1995, to expense certain subscriber acquisition costs as incurred.

Results of Operations

Fiscal 1995 Compared to Fiscal 1994

Online Service Revenues For fiscal 1995, online service revenues increased from $100,993,000 to $358,498,000, or 255%, over fiscal 1994. This increase was primarily attributable to a 289% increase in revenues from IBM-compatible subscribers and a 196% increase in revenues from Macintosh subscribers as a result of a 273% increase in the number of IBM-compatible subscribers and a 143% increase in the number of Macintosh subscribers. The percentage increase in online service revenues in fiscal 1995 was greater than the percentage increase in subscribers principally due to an increase in the average monthly online service revenue per

subscriber, which increased from $15.00 in fiscal 1994 to $17.10 in fiscal 1995.

Other Revenues Other revenues, consisting principally of new media and interactive marketing services, data network services, multimedia and CD-ROM production services, and development and licensing fees, increased from $14,729,000 in fiscal 1994 to $35,792,000 in fiscal 1995. This increase was primarily attributable to data network revenues and multimedia and CD-ROM production service revenues from companies acquired during fiscal 1995.

Cost of Revenues Cost of revenues includes network-related costs, consisting primarily of data and voice communication costs, costs associated with operating the data center and providing customer support, royalties paid to information and service providers and other expenses related to marketing and production services. For fiscal 1995, cost of revenues increased from $69,043,000 to $229,724,000, or 233%, over fiscal 1994, and decreased as a percentage of total revenues from 59.7% to 58.3%.

The increase in cost of revenues was primarily attributable to an increase in data communication costs, customer support costs and royalties paid to information and service providers. Data communication costs increased primarily as a result of the larger customer base and more usage by customers. Customer support costs, which include personnel and telephone costs associated with providing customer support, were higher as a result of the larger customer base and a large number of new subscriber registrations. Royalties paid to information and service providers increased as a result of a larger customer base and more usage and the Company's addition of more service content to broaden the appeal of the America Online service.

The decrease in cost of revenues as a percentage of total revenues is primarily attributable to a decrease in expenses related to marketing services and personnel related costs as a percentage of total revenues, partially offset by an increase in data communication costs as a percentage of total revenues, primarily resulting from an increase in higher baud speed usage at a higher variable rate as well as lower hourly pricing for online service revenue which became effective January 1, 1995.

Marketing Marketing expenses include the costs to acquire and retain subscribers and other general marketing expenses. Subscriber acquisition costs are deferred and charged to operations over a twelve or eighteen month period, using the straight-line method, beginning the month after such costs are incurred. For additional information regarding the accounting for deferred subscriber acquisition costs, refer to Note 2 of the Notes to Consolidated Financial Statements. For fiscal 1995, marketing expenses increased from $23,548,000 to $77,064,000, or 227%, over fiscal 1994, and decreased as a percentage of total revenues from 20.3% to 19.5%. The increase in marketing expenses was primarily due to an increase in the number and size of marketing programs to expand the Company's subscriber base. The decrease in marketing expenses as a percentage of total revenues is primarily attributable to a decrease as a percentage of total revenues in personnel related costs.

Product Development Product development costs include research and development expenses, other product development costs and the amortization of software costs. For fiscal 1995, product development expenses increased from $4,961,000 to $12,842,000, or 159%, over fiscal 1994, and decreased as a percentage of total revenues from 4.3% to 3.3%. The increase in product development costs was primarily attributable to an increase in personnel costs related to an increase in the number of technical employees. The decrease in product development costs as a percentage of total revenues was principally a result of the substantial growth in revenues, which more than offset the additional product development costs. Product development costs, before capitalization and amortization, increased by 126% in fiscal 1995.

General and Administrative For fiscal 1995, general and administrative costs increased from $13,562,000 to $41,966,000, or 209%, over fiscal 1994, and decreased as a percentage of total revenues from 11.7% to 10.6%. The increase in general and administrative expenses was principally attributable to higher office and personnel expenses related to an increase in the number of employees. The decrease in general and administrative costs as a percentage of total revenues was a result of the substantial growth in revenues, which more than offset the additional general and administrative costs, combined with the semi-variable nature of many of the general and administrative costs.

Acquired Research and Development Acquired research and development costs, totaling $50,335,000, relate to in-process research and development purchased pursuant to the Company's acquisitions of two early-stage Internet technology companies, BookLink and NaviSoft. The purchased research and development relating to the BookLink and NaviSoft acquisitions was the foundation of the development of the Company's Internet related products.

Amortization of Goodwill Amortization of goodwill relates to the Company's acquisition of ANS, which resulted in approximately $44 million in goodwill. The goodwill related to the ANS acquisition is being amortized on a straight-line basis over a ten year period.

Other Income Other income consists primarily of investment and rental income net of interest expense. For fiscal 1995, other income increased from $1,774,000 to $3,023,000.

This increase was primarily attributable to an increase in interest income generated by higher levels of cash available for investment, partially offset by a decrease in rental income and an increase in interest expense.

Merger Expenses Non-recurring merger expenses totaling $2,207,000 were recognized in fiscal 1995 in connection with the mergers of the Company with RCC, WAIS and Medior.

Provision for Income Taxes The provision for income taxes was $3,832,000 and $15,169,000 in fiscal 1994 and fiscal 1995, respectively. For additional information regarding income taxes, refer to Note 9 of the Notes to Consolidated Financial Statements.

Net Loss The net loss in fiscal 1995 totaled $33,647,000. The net loss in fiscal 1995 included charges of $50,335,000 for acquired research and development and $2,207,000 for merger expenses.

Fiscal 1994 Compared to Fiscal 1993

Online Service Revenues For fiscal 1994, online service revenues increased from $38,462,000 to $100,993,000, or 163%, over fiscal 1993. This increase was primarily attributable to a 198% increase in revenues from IBM-compatible subscribers and a 145% increase in revenues from Macintosh subscribers as a result of a 230% increase in the number of IBM-compatible subscribers and a 174% increase in the number of Macintosh subscribers. The percentage increase in subscribers in fiscal 1994 was greater than the percentage increase in online service revenues due to the timing, during the year, of when subscribers were added. The majority of subscribers were added during the second half of the year, therefore there was not a full year impact on revenues. This was partially offset by an increase in average monthly net service revenue per subscriber, which increased from $14.20 in fiscal 1993 to $15.00 in fiscal 1994.

Other Revenues Other revenues, consisting primarily of new media and interactive marketing services and development fees, increased from $13,522,000 in fiscal 1993 to $14,729,000 in fiscal 1994.

Cost of Revenues For fiscal 1994, cost of revenues increased from $28,820,000 to $69,043,000, or 140%, over fiscal 1993, and increased as a percentage of total revenues from 55.4% to 59.7%.

The increase in cost of revenues was primarily attributable to an increase in data communication costs, customer support costs and royalties paid to information and service providers. Data communication costs increased primarily as a result of the larger customer base and more usage by customers. Customer support costs, which include personnel and telephone costs associated with providing customer support, were higher as a result of the larger customer base and a large number of new subscriber registrations. Royalties paid to information and service providers increased as a result of a larger customer base and more usage and the Company adding more service content to broaden the appeal of the America Online service.

The increase in cost of revenues as a percentage of total revenues is primarily attributable to data communication costs and is associated with (i) an increase in no-charge trial hours as a result of the high number of new subscriber registrations relative to the existing customer base; (ii) a higher percentage of usage during more costly daytime periods partially offset by more favorable pricing under an agreement with the Company's primary communications provider; and (iii) an increase in usage relative to net service revenues as a result of the introduction of a price change in May 1993. The increase attributable to data communications costs was partially offset by a decrease as a percentage of total revenues in production costs related to marketing services. The Company introduced a price change in the spring of 1993. Prior thereto, the Company's standard pricing was a monthly membership fee of $7.95 which included two hours of use each month, with five no-charge trial hours and no membership fee in the first month. Additional usage beyond that included with the membership was charged at $6.00 per hour. Effective May 1, 1993, the Company increased the monthly membership fee to $9.95 and increased the number of hours included to five per month. Additionally, the number of no-charge trial hours in the first month of membership was increased from five to ten. Effective July 1, 1993, the hourly fee for usage beyond that included with the membership was lowered to $3.50.

Marketing For fiscal 1994, marketing expenses increased from $9,745,000 to $23,548,000, or 142%, over fiscal 1993, and increased as a percentage of total revenues from 18.7% to 20.3%. The increase in marketing expenses was primarily due to an increase in the number and size of marketing programs to expand the Company's America Online subscriber base. In addition, personnel costs were higher to support the number and size of marketing programs.

Product Development For fiscal 1994, product development costs increased from $2,913,000 to $4,961,000, or 70%, over fiscal 1993, and decreased as a percentage of total revenues from 5.6% to 4.3%. The increase in product development costs was attributable to an increase in personnel costs related to an increase in the number of employees. The decrease in product development costs as a percentage of total revenues was a result of the substantial growth in revenues for the year, which more than offset the additional

product development costs. Product development costs, before capitalization and amortization, increased by 103% in fiscal 1994.

General and Administrative For fiscal 1994, general and administrative expenses increased from $8,581,000 to $13,562,000, or 58%, over fiscal 1993, and decreased as a percentage of total revenues from 16.5% to 11.7%. The increase in general and administrative costs was principally attributable to higher personnel, office and travel expenses related to an increase in the number of employees. The decrease in general and administrative costs as a percentage of total revenues was a result of the substantial growth in revenues for the year combined with the fixed nature of many of the general and administrative costs.

Other Income For fiscal 1994, other income increased from $371,000 to $1,774,000. This increase was primarily attributable to an increase in interest income generated by higher levels of cash available for investment in fiscal 1994, as well as rental income received as a result of the purchase of one of the Company's office buildings and its leasing of space to third parties, which was partially offset by interest expense on the loan obtained to purchase the building.

Provision for Income Taxes The provision for income taxes was $1,897,000 and $3,832,000 in fiscal 1993 and fiscal 1994, respectively. The tax provision in fiscal 1993, with the exception of $764,000, was offset by the utilization of a net operating loss carryforward that has been reflected as an extraordinary item. For additional information regarding income taxes, refer to Note 9 of the Notes to Consolidated Financial Statements.

Net Income Net income in fiscal 1994 totaled $2,550,000.

Liquidity and Capital Resources

The Company has financed its operations through cash generated from operations, sale of its common stock and funding by third parties for certain product development activities. Net cash provided by operating activities was $2,205,000, $1,884,000 and $15,891,000 for fiscal 1993, fiscal 1994 and fiscal 1995, respectively. Included in operating activities were expenditures for deferred acquisition costs of $10,685,000, $37,424,000 and $111,761,000 in fiscal 1993, fiscal 1994 and fiscal 1995, respectively. Net cash used in investing activities was $8,915,000, $41,870,000 and $85,725,000 in fiscal 1993, fiscal 1994 and fiscal 1995, respectively. Investing activities included $20,523,000 in fiscal 1995 related to business acquisitions, substantially all of which was related to the acquisition of ANS.

In December 1993 the Company completed a public stock offering of 4,000,000 shares of common stock which generated net cash proceeds of approximately $62.7 million.

In April 1995 the Company entered into a joint venture with Bertelsmann, AG ("Bertelsmann") to offer interactive online services in Europe. In connection with the agreement, the Company received approximately $54 million through the sale of approximately 5% of its common stock to Bertelsmann.

The Company leases the majority of its equipment under noncancelable operating leases, and as part of its network portfolio strategy is building AOLnet, its data communications network. The buildout of this network requires a substantial investment in telecommunications equipment, which the Company plans to finance principally through leasing. In addition, the Company has guaranteed minimum commitments under certain data and voice communication agreements. The Company's future lease commitments and guaranteed minimums are discussed in Note 6 of the Notes to Consolidated Financial Statements.

The Company uses its working capital to finance ongoing operations and to fund marketing and content programs and the development of its products and services. The Company plans to continue to invest aggressively in acquisition marketing and content programs to expand its subscriber base, as well as in computing and support infrastructure. Additionally, the Company expects to use a portion of its cash for the acquisition and subsequent funding of technologies, products or businesses complementary to the Company's current business. Apart from its agreement to acquire Ubique, as discussed below, the Company has no agreements or understandings to acquire any businesses. The Company anticipates that available cash and cash provided by operating activities will be sufficient to fund its operations for the next fiscal year.

Various legal proceedings have arisen against the Company in the ordinary course of business. In the opinion of management, these proceedings will not have a material effect on the financial position of the Company.

The Company believes that inflation has not had a material effect on its results of operations.

On August 23, 1995, the Company entered into a stock purchase agreement to purchase Ubique, an Israeli company. The Company has agreed to pay approximately $15 million ($1.5 million in cash and $13.5 million in common stock) in the transaction, which is to be accounted for as a purchase. Subject to the result of an in-process valuation, a substantial portion of the purchase price may be allocated to in-process research and development and charged to the Company's operations in the first quarter of fiscal 1996.

Consolidated Statements of Operations

(Amounts in thousands, except per share data)	Year ended June 30, 1995	1994	1993
Revenues:			
Online service revenues	$ 358,498	$ 100,993	$ 38,462
Other revenues	35,792	14,729	13,522
Total revenues	394,290	115,722	51,984
Costs and expenses:			
Cost of revenues	229,724	69,043	28,820
Marketing	77,064	23,548	9,745
Product development	12,842	4,961	2,913
General and administrative	41,966	13,562	8,581
Acquired research and development	50,335	–	–
Amortization of goodwill	1,653	–	–
Total costs and expenses	413,584	111,114	50,059
Income (loss) from operations	(19,294)	4,608	1,925
Other income, net	3,023	1,774	371
Merger expenses	(2,207)	–	–
Income (loss) before provision for income taxes and extraordinary item	(18,478)	6,382	2,296
Provision for income taxes	(15,169)	(3,832)	(1,897)
Income (loss) before extraordinary item	(33,647)	2,550	399
Extraordinary item - tax benefit arising from net operating loss carryforward	–	–	1,133
Net income (loss)	$ (33,647)	$ 2,550	$ 1,532
Earnings (loss) per share:			
Income (loss) before extraordinary item	$ (0.99)	$ 0.07	$ 0.01
Net income (loss)	$ (0.99)	$ 0.07	$ 0.05
Weighted average shares outstanding	33,986	34,208	29,286

See accompanying notes.

Consolidated Balance Sheets

(Amounts in thousands, except share data)	June 30, 1995	1994
Assets		
Current assets:		
Cash and cash equivalents	$ 45,378	$ 43,891
Short-term investments	18,672	24,052
Trade accounts receivable	32,176	8,547
Other receivables	11,103	2,036
Prepaid expenses and other current assets	25,527	5,753
Total current assets	132,856	84,279
Property and equipment at cost, net	70,466	20,306
Other assets:		
Product development costs, net	18,914	7,912
Deferred subscriber acquisition costs, net	77,229	26,392
License rights, net	5,537	53
Other assets	11,479	2,800
Deferred income taxes	35,627	12,842
Goodwill, net	54,356	–
	$406,464	$ 154,584
Liabilities And Stockholders' Equity		
Current liabilities:		
Trade accounts payable	$ 84,639	$ 15,642
Accrued personnel costs	2,829	896
Other accrued expenses and liabilities	23,509	13,076
Deferred revenue	20,021	4,488
Line of credit	484	1,690
Current portion of long-term debt and capital lease obligations	1,830	597
Total current liabilities	133,312	36,389
Long-term liabilities:		
Notes payable	17,369	5,836
Capital lease obligations	2,127	1,179
Deferred income taxes	35,627	12,842
Deferred rent	85	41
Total liabilities	188,520	56,287
Stockholders' equity:		
Preferred stock, $.01 par value; 5,000,000 shares authorized, none issued	–	–
Common stock, $.01 par value; 100,000,000 shares authorized, 37,554,849 and 30,771,212 shares issued and outstanding at June 30, 1995 and 1994, respectively	375	308
Additional paid-in capital	251,539	98,836
Accumulated deficit	(33,970)	(847)
Total stockholders' equity	217,944	98,297
	$406,464	$ 154,584

See accompanying notes.

Consolidated Statements of Changes in Stockholders' Equity

(Amounts in thousands, except share data)

	Common Stock		Additional	Accumulated	
	Shares	Amount	Paid-in Capital	Deficit	Total
Balances at June 30, 1992	23,135,780	$ 231	$ 26,250	$ (4,870)	$ 21,611
Exercise of common stock options and warrants	1,645,288	16	568	–	584
Other	–	–	111	(59)	52
Tax benefit related to stock options	–	–	6	–	6
Net income	–	–	–	1,532	1,532
Balances at June 30, 1993	24,781,068	247	26,935	(3,397)	23,785
Common stock issued:					
Exercise of options and warrants	1,413,640	14	1,850	–	1,864
Sale of stock, net	4,576,504	47	65,461	–	65,508
Tax benefit related to stock options	–	–	4,590	–	4,590
Net income	–	–	–	2,550	2,550
Balances at June 30, 1994	30,771,212	308	98,836	(847)	98,297
Effect of immaterial poolings	1,031,378	10	1,043	524	1,577
Balances as restated	31,802,590	318	99,879	(323)	99,874
Common stock issued:					
Exercise of options	1,452,628	14	4,670	–	4,684
Business acquisitions	2,392,677	24	75,677	–	75,701
Sale of stock, net	1,906,954	19	56,550	–	56,569
Tax benefit related to stock options	–	–	14,763	–	14,763
Net loss	–	–	–	(33,647)	(33,647)
Balances at June 30, 1995	**37,554,849**	**$ 375**	**$251,539**	**$ (33,970)**	**$217,944**

See accompanying notes.

Consolidated Statements of Cash Flows

(Amounts in thousands)	Year ended June 30,		
	1995	1994	1993
Cash flows from operating activities:			
Net income (loss)	**$ (33,647)**	$ 2,550	$ 1,532
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	**11,136**	2,965	1,957
Amortization of subscriber acquisition costs	**60,924**	17,922	7,038
Loss/(Gain) on sale of property and equipment	**37**	5	(39)
Charge for acquired research and development	**50,335**	–	–
Changes in assets and liabilities:			
Trade accounts receivable	**(14,373)**	(4,266)	(936)
Other receivables	**(9,057)**	(681)	(966)
Prepaid expenses and other current assets	**(19,641)**	(2,867)	(1,494)
Deferred subscriber acquisition costs	**(111,761)**	(37,424)	(10,685)
Other assets	**(8,432)**	(2,519)	(89)
Trade accounts payable	**60,824**	10,204	2,119
Accrued personnel costs	**1,846**	367	336
Other accrued expenses and liabilities	**5,703**	9,526	1,492
Deferred revenue	**7,190**	2,322	1,381
Deferred income taxes	**14,763**	3,832	759
Deferred rent	**44**	(52)	(200)
Total adjustments	**49,538**	(666)	673
Net cash provided by operating activities	**15,891**	1,884	2,205
Cash flows from investing activities:			
Short-term investments	**5,380**	(18,947)	(5,105)
Purchase of property and equipment	**(57,751)**	(17,886)	(2,041)
Product development costs	**(13,011)**	(5,132)	(1,831)
Sale of property and equipment	**180**	95	62
Purchase costs of acquired businesses	**(20,523)**	–	–
Net cash used in investing activities	**(85,725)**	(41,870)	(8,915)
Cash flows from financing activities:			
Proceeds from issuance of common stock, net	**61,253**	67,372	609
Principal and accrued interest payments on line of credit and long-term debt	**(3,298)**	(7,716)	(6,924)
Proceeds from line of credit and issuance of long-term debt	**13,741**	14,200	7,181
Tax benefit from stock option exercises	**–**	–	6
Principal payments under capital lease obligations	**(375)**	(142)	(112)
Net cash provided by financing activities	**71,321**	73,714	760
Net increase (decrease) in cash and cash equivalents	**1,487**	33,728	(5,950)
Cash and cash equivalents at beginning of period	**43,891**	10,163	16,113
Cash and cash equivalents at end of period	**$ 45,378**	$ 43,891	$ 10,163
Supplemental cash flow information			
Cash paid during the period for:			
Interest	**1,067**	575	193
Income taxes	**–**	–	15

See accompanying notes.

Notes to Consolidated Financial Statements

1 Organization

America Online, Inc. ("the Company"), was incorporated in the State of Delaware in May 1985. The Company, based in Vienna, Virginia, is a leading provider of online services, offering its subscribers a wide variety of services, including e-mail, online conferences, entertainment, software, computing support, interactive magazines and newspapers, and online classes, as well as easy and affordable access to services of the Internet. In addition, the Company is a provider of data network services, new media and interactive marketing services, and multimedia and CD-ROM production services.

2 Summary of Significant Accounting Policies

Principles of Consolidation The consolidated financial statements include the accounts of the Company and its subsidiaries. All significant intercompany accounts and transactions have been eliminated. Investments in affiliates owned twenty percent or more and corporate joint ventures are accounted for under the equity method. Other securities in companies owned less than twenty percent are accounted for under the cost method.

Business Combinations Business combinations which have been accounted for under the purchase method of accounting include the results of operations of the acquired business from the date of acquisition. Net assets of the companies acquired are recorded at their fair value to the Company at the date of acquisition.

Other business combinations have been accounted for under the pooling of interests method of accounting. In such cases, the assets, liabilities, and stockholders' equity of the acquired entities were combined with the Company's respective accounts at recorded values. Prior period financial statements have been restated to give effect to the merger unless the effect of the business combination is not material to the financial statements of the Company.

Revenue and Cost Recognition Online service revenue is recognized over the period services are provided. Other revenue, consisting principally of marketing, data network and multimedia production services, as well as development and royalty revenues, are recognized as services are rendered. Deferred revenue consists principally of third-party development funding not yet recognized and monthly subscription fees billed in advance.

Property and Equipment Property and equipment are depreciated or amortized using the straight-line method over the estimated useful life of the asset, which ranges from 5 to 40 years, or over the life of the lease.

Property and equipment under capital leases are stated at the lower of the present value of minimum lease payments at the beginning of the lease term or fair value at inception of the lease.

Deferred Subscriber Acquisition Costs Subscriber acquisition costs are deferred and charged to operations over a twelve or eighteen month period (straight-line method) beginning the month after such costs are incurred. These costs, which relate directly to subscriber solicitations, principally include printing, production and shipping of starter kits and the costs of obtaining qualified prospects by various targeted direct marketing programs (i.e., direct marketing response cards, mailing lists) and from third parties, are recorded separately from ordinary operating expenses. No indirect costs are included in subscriber acquisition costs. To date, all subscriber acquisition costs have been incurred for the solicitation of specific identifiable prospects. Costs incurred for other than those targeted at specific identifiable prospects for the Company's services, and general marketing, are expensed as incurred.

The Company's services are sold on a monthly subscription basis. Subscriber acquisition costs incurred to obtain new subscribers are recoverable from revenues generated by such subscribers within a short period of time after such costs are incurred.

Effective July 1, 1992, the Company changed, from twelve months to eighteen months, the period over which it amortizes the cost of deferred subscriber acquisition costs relating to marketing activities in which the Company's starter kit is bundled and distributed by a third-party marketing company. The change in accounting estimate was made to more accurately match revenues and expenses. Based on the Company's experience and the distribution channels used in such marketing activities, there is a greater time lag between the time the Company incurs the cost for the starter kits and the time the starter kits begin to generate new customers than with direct marketing activities. Also, the period over which new subscribers (and related revenues) are generated is longer than that experienced with the use of traditional

independent, direct marketing activities. The effect of this change in accounting estimate for the year ended June 30, 1993 was to increase income before extraordinary item and net income by $264,000 ($.01 per share).

In the first quarter of fiscal 1995 the Company adopted the provisions of Statement of Position ("SOP") 93-7 "Reporting on Advertising Costs" which provides guidance on financial reporting on advertising costs. The adoption of SOP 93-7 had no effect on the Company's financial position or results of operations.

Product Development Costs The Company capitalizes costs incurred for the production of computer software used in the sale of its services. Costs capitalized include direct labor and related overhead for software produced by the Company and the costs of software purchased from third parties. All costs in the software development process which are classified as research and development are expensed as incurred until technological feasibility has been established. Once technological feasibility has been established, such costs are capitalized until the software is commercially available. To the extent the Company retains the rights to software development funded by third parties, such costs are capitalized in accordance with the Company's normal accounting policies. Amortization is provided on a product-by-product basis, using the greater of the straight-line method or current year revenue as a percent of total revenue estimates for the related software product not to exceed five years, commencing the month after the date of product release.

Product development costs consist of the following:

(in thousands)	Year ended June 30, 1995	1994
Balance, beginning of year	**$ 7,912**	$ 3,915
Costs capitalized	**13,011**	5,132
Costs amortized	**(2,009)**	(1,135)
Balance, end of year	**$18,914**	$ 7,912

The accumulated amortization of product development costs related to the production of computer software totaled $7,894,000, and $5,885,000 at June 30, 1995 and 1994, respectively.

Included in product development costs are research and development costs totaling $3,856,000, $2,126,000, and $1,130,000 and other product development costs totaling $6,977,000, $1,050,000 and $579,000 in the years ended June 30, 1995, 1994 and 1993, respectively.

License Rights The cost of acquired license rights is amortized using the straight-line method over the term of the agreement for such license rights, ranging from one to three years.

Goodwill Goodwill consists of the excess of cost over the fair value of net assets acquired and certain other intangible assets relating to purchase transactions. Goodwill and intangible assets are amortized over periods ranging from 5 - 10 years.

Operating Lease Costs Rent expense for operating leases is recognized on a straight-line basis over the lease term. The difference between rent expense incurred and rental payments is charged or credited to deferred rent.

Cash, Cash Equivalents and Short-term Investments The Company considers all highly liquid investments with an original maturity of three months or less to be cash equivalents. In fiscal 1995, the Company adopted Statement of Financial Accounting Standards No. 115 ("SFAS 115"), "Accounting for Certain Investments in Debt and Equity Securities." The adoption was not material to the Company's financial position or results of operations. The Company has classified all debt and equity securities as available-for-sale. Available-for-sale securities are carried at fair value, with unrealized gains and losses reported as a separate component of stockholders' equity. Realized gains and losses and declines in value judged to be other-than-temporary on available-for-sale securities are included in other income. Available-for-sale securities at June 30, 1995, consisted of U.S. Treasury Bills and other obligations of U.S. Government agencies totaling $7,579,000 and U.S. corporate debt obligations totaling $11,093,000. At June 30, 1995, the estimated fair value of these securities approximated cost.

Net Income (Loss) per Common Share Net income (loss) per share is calculated by dividing income (loss) before extraordinary item and net income (loss) by the weighted average number of common and, when dilutive, common equivalent shares outstanding during the period.

Reclassification Certain amounts in prior years' consolidated financial statements have been reclassified to conform to the current year presentation.

3 Business Combinations

Pooling Transactions On August 19, 1994, Redgate Communications Corporation ("RCC") was merged with and

into a subsidiary of the Company. The Company exchanged 1,789,300 shares of common stock for all of the outstanding common and preferred stock and warrants of RCC. Additionally, 401,148 shares of the Company's common stock were reserved for outstanding stock options issued by RCC and assumed by the Company. The merger was accounted for under the pooling of interests method of accounting, and accordingly, the accompanying consolidated financial statements have been restated for all periods prior to the acquisition to include the financial position, results of operations and cash flows of RCC. Effective August 1994, RCC's fiscal year-end has been changed from December 31 to June 30 to conform to the Company's fiscal year-end.

Revenues and net earnings (loss) for the individual entities are as follows:

(in thousands)	Three months ended September 30, (unaudited)	Year ended June 30,	
	1994	1994	1993
Total revenues:			
AOL	$ 50,783	$104,410	$ 40,019
RCC	3,813	11,312	11,965
Less intercompany sales	(173)	–	–
	$ 54,423	$115,722	$ 51,984
Net income (loss):			
AOL	$ 3,018	$ 6,210	$ 4,210
RCC	(42)	(3,660)	(2,678)
Merger expenses	(1,710)	–	–
	$ 1,266	$ 2,550	$ 1,532

In connection with the merger of the Company and RCC, merger expenses of $1,710,000 were recognized during 1995.

During fiscal 1995, Medior, Inc. and Wide Area Information Servers, Inc. were merged into subsidiaries of the Company. The Company issued 1,082,019 shares of its common stock in the transactions. The transactions were accounted for under the pooling of interests method of accounting. Prior year financial statements have not been restated for the transactions because the effect would not be material to the operations of the Company.

Purchase Transactions During fiscal 1995, the Company acquired NaviSoft, Inc. ("NaviSoft"), BookLink Technologies, Inc. ("BookLink"), Advanced Network & Services, Inc. ("ANS") and Global Network Navigator, Inc., in transactions accounted for under the purchase method of accounting. The Company paid a total of $97,669,000 of which $75,697,000 was in stock and $21,972,000 was in cash for the acquisitions. Of the aggregate purchase price, approximately $50,335,000 was allocated to in-process research and development and $55,314,000 was allocated to goodwill and other intangible assets.

The following unaudited pro forma information relating to the BookLink and ANS acquisitions is not necessarily an indication of the combined results that would have occurred had the acquisitions taken place at the beginning of the period, nor is it necessarily an indication of the results that may occur in the future. Pro forma information for NaviSoft and Global Network Navigator, Inc. is immaterial to the operations of the consolidated entity. The amount of the aggregate purchase price allocated to in-process research and development for both the NaviSoft and BookLink acquisitions has been excluded from the pro forma information as it is a non-recurring item.

(in thousands, except per share data)	Year ended June 30,	
	1995	1994
Revenues	**$410,147**	$135,785
Income (loss) from operations	**23,117**	(5,465)
Pro forma income (loss)	**11,205**	(4,694)
Pro forma income (loss) per share	**$ 0.25**	$ (0.16)

4 Property and Equipment

Property and equipment consist of the following:

(in thousands)	June 30,	
	1995	1994
Computer equipment	**$ 49,167**	$ 12,418
Furniture and fixtures	**4,992**	1,398
Buildings	**13,800**	5,648
Land	**6,075**	2,052
Building improvements	**6,284**	1,343
Property under capital leases	**8,486**	2,686
Leasehold improvements	**3,059**	306
	91,863	25,851
Less accumulated depreciation and amortization	**21,397**	5,545
Net property and equipment	**$ 70,466**	$ 20,306

5 License Rights

License rights consist of the following:

(in thousands)	June 30, 1995	June 30, 1994
License rights	$ 7,484	$ 954
Less accumulated amortization	(1,947)	(901)
	$ 5,537	$ 53

6 Commitments and Contingencies

The Company leases equipment under several long-term capital and operating leases. Future minimum payments under capital leases and non cancelable operating leases with initial terms of one year or more consist of the following:

(in thousands) Year ending June 30,	Capital Leases	Operating Leases
1996	$ 1,654	$ 20,997
1997	1,236	21,264
1998	641	19,450
1999	310	8,711
2000	103	3,511
Thereafter	–	2,636
Total minimum lease payments	3,944	$ 76,569
Less amount representing interest	(402)	
Present value of net minimum capital lease payments, including current portion of $1,415	$ 3,542	

The Company's rental expense under operating leases in the years ended June 30, 1995, 1994 and 1993 totaled approximately $10,001,000, $2,889,000, and $2,155,000, respectively.

Communication Networks The Company has guaranteed monthly usage levels of data and voice communications with one of its vendors. The remaining commitments are $113,400,000, $59,000,000, $9,000,000 and $6,750,000 for the years ending June 30, 1996, 1997, 1998 and 1999, respectively. The related expense for the years ended June 30, 1995, 1994 and 1993 was $138,793,000, $40,315,000 and $11,226,000, respectively.

Contingencies Various legal proceedings have arisen against the Company in the ordinary course of business. In the opinion of management, these proceedings will not have a material effect on the financial position of the Company.

7 Notes Payable

Notes payable at June 30, 1995 totaled approximately $18 million and consist primarily of amounts borrowed to finance the purchases of two office buildings. The notes are collateralized by the respective properties. The notes have a variable interest rate equal to 105 basis points above the 30 day London Interbank Offered Rate and a fixed interest rate of 8.48% per annum at June 30, 1995. Aggregate maturities of notes payable for the years ended June 30, 1996, 1997, 1998, 1999, 2000 and thereafter are $415,000, $429,000, $445,000, $462,000, $480,000 and $15,553,000, respectively.

8 Other Income

The following table summarizes the components of other income:

(in thousands)	Year ended June 30, 1995	1994	1993
Interest income	$ 3,920	$ 1,646	$ 572
Interest expense	(1,054)	(575)	(172)
Other	157	703	(29)
	$ 3,023	$ 1,774	$ 371

9 Income Taxes

The provision for income taxes is attributable to:

(in thousands)	Year ended June 30, 1995	1994	1993
Income before extraordinary item	$ 15,169	$ 3,832	$ 1,897
Tax benefit arising from net operating loss carryforward	–	–	(1,133)
	$ 15,169	$ 3,832	$ 764
Current	$ –	$ –	$ 5
Deferred	15,169	3,832	759
	$ 15,169	$ 3,832	$ 764

The provision for income taxes differs from the amount computed by applying the statutory federal income tax rate to income before provision for income taxes and extraordinary item. The sources and tax effects of the differences are as follows:

(in thousands)	Year ended June 30, 1995	1994	1993
Income tax at the federal statutory rate of 34%	$ (6,283)	$ 2,170	$ 781
State income tax, net of federal benefit	1,597	403	200
Losses relating to RCC	–	1,259	916
Nondeductible merger expenses	750	–	–
Nondeductible charge for purchased research and development	17,114	–	–
Loss, for which no tax benefit was derived	1,632	–	–
Other	359	–	–
	$ 15,169	$ 3,832	$ 1,897

Deferred income taxes arise because of differences in the treatment of income and expense items for financial reporting and income tax purposes, primarily relating to deferred subscriber acquisition and product development costs.

As of June 30, 1995, the Company has net operating loss carryforwards of approximately $109 million for tax purposes which will be available, subject to certain annual limitations, to offset future taxable income. If not used, these loss carryforwards will expire between 2001 and 2010. To the extent that net operating loss carryforwards, when realized, relate to stock option deductions, the resulting benefits will be credited to stockholders' equity.

The Company's income tax provision was computed based on the federal statutory rate and the average state statutory rates, net of the related federal benefit.

Effective July 1, 1993 the Company changed its method of accounting for income taxes from the deferred method to the liability method required by FASB Statement No. 109, "Accounting for Income Taxes." As permitted under the new rules, prior years' financial statements have not been restated.

No increase to net income resulted from the cumulative effect of adopting Statement No. 109 as of July 1, 1993. The deferred tax asset increased by approximately $5,965,000 as a result of the adoption. Similarly, the deferred tax liability, stockholders' equity and the valuation allowance increased by approximately $3,173,000, $759,000 and $2,033,000, respectively.

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company's deferred tax liabilities and assets are as follows:

(in thousands)	June 30, 1995	1994
Deferred tax liabilities:		
Capitalized software costs	$ 7,008	$ 2,962
Deferred member acquisition costs	28,619	9,880
Net deferred tax liabilities	$ 35,627	$ 12,842
Deferred tax assets:		
Net operating loss carryforwards	$ 39,000	$ 17,510
Total deferred tax assets	39,000	17,510
Valuation allowance for deferred assets	(3,373)	(4,668)
Net deferred tax assets	$ 35,627	$ 12,842

10 Capital Accounts

Common Stock At June 30, 1995 and 1994 the Company's $.01 par value common stock authorized was 100,000,000 and 20,000,000 shares, respectively, with 37,544,849 and 30,771,212 shares issued and outstanding, respectively. At June 30, 1995, 23,778,605 shares were reserved for the exercise of issued and unissued common stock options and warrants, and 289,115 shares were reserved for issuance in connection with the Company's Employee Stock Purchase Plan.

During April 1995, the Company sold approximately 5% of its common stock for approximately $54 million to Bertelsmann, AG in connection with a joint venture.

Preferred Stock In February 1992, the Company's stockholders approved an amendment and restatement of the certificate of incorporation which authorized the future issuance of 5,000,000 shares of preferred stock, $.01 par value, with rights and preferences to be determined by the Board of Directors. As of June 30, 1995 no shares of preferred stock had been issued.

Warrants Under a December 1992 licensing and development agreement with Apple Computer, Inc. ("Apple"), the Company issued warrants to Apple to purchase 2,000,000 shares of common stock at an exercise price of $6.25 per share.

In connection with an agreement with the Company's primary communications provider, the Company issued warrants, exercisable through March 31, 1999, subject to certain performance standards specified in the agreement, to purchase 1,800,000 shares of common stock at a price of $7.81 per share.

Shareholder Rights Plan During fiscal 1993, the Company adopted a shareholder rights plan and distributed a dividend of one preferred share purchase right (a "Right") for each outstanding share of the Company's common stock. The Rights become exercisable in certain limited circumstances involving a potential business combination or change of control transaction of the Company. Each Right initially entitles registered holders of the Company's common stock to purchase one one-hundredth of a share of the Company's new Series A Junior Participating Preferred Stock ("Series A Preferred Stock") at a price of $150.00 per one one-hundredth of a share of Series A Preferred Stock. Following certain other events after the Rights have become exercisable, each Right entitles its holder to purchase for $150.00 an amount of common stock of the Company or, in certain circumstances, securities of the acquirer, having a then-current market value of two times the exercise price of the Right. The Rights are redeemable for one cent per right at the option of the Board of Directors. Until a Right is exercised, the holder of the Right, as such, has no rights as a shareholder of the Company. The Rights expire on May 3, 2003 unless redeemed prior to that date.

Stock Splits On November 25, 1994 and April 27, 1995, the Company effected two-for-one splits of the outstanding shares of common stock. Accordingly, all data shown in the accompanying consolidated financial statements and notes has been retroactively adjusted to reflect the stock splits.

11 Stock Plans

Incentive Stock Option Plan In June 1985, the Company approved and adopted an incentive stock option plan ("the 1985 Plan"). The 1985 Plan provides for the grant of options to purchase common stock to eligible employees of the Company. The 1985 Plan is administered by the Compensation Committee of the Board of Directors. The 1985 Plan will terminate in December 1995. The total number of shares of common stock that may be issued pursuant to options granted under the 1985 Plan is 3,002,872. The issued options vest over three-year or four-year periods and are exercisable for ten years following the date of the grant.

The following table summarizes incentive stock option activity under the 1985 Plan:

	Number of shares	Option price per share
Balance at June 30, 1992	2,191,844	$0.12 - $2.25
Granted	–	–
Exercised	(403,236)	$0.12 - $2.25
Forfeited	(14,240)	$2.25
Balance at June 30, 1993	1,774,368	$0.12 - $2.25
Granted	–	–
Exercised	(470,216)	$0.12 - $2.25
Forfeited	(2,200)	$2.25
Balance at June 30, 1994	1,301,952	$0.12 - $2.25
Granted	–	–
Exercised	(258,770)	$0.12 - $2.25
Forfeited	(30,650)	$2.25
Balance at June 30, 1995	1,012,532	$0.12 - $2.25

At June 30, 1995, 893,192 options were exercisable. There have been 1,940,786 options exercised under the 1985 Plan.

Stock Incentive Plan In December 1987, the Company's Board of Directors adopted a stock incentive plan ("the 1987 Plan"). The 1987 Plan provides for the grant of options to purchase common stock and awards of restricted common stock to employees and independent contractors of the Company. The 1987 Plan is administered by the Compensation Committee of the Board of Directors. The total number of shares of common stock that may be issued pursuant to options granted under the 1987 Plan or pursuant to stock awards is 4,008,000. The issued options vest over three-, four- or five-year periods and are exercisable for ten years following the date of grant.

The following table summarizes stock incentive option activity under the 1987 Plan:

	Number of shares	Option price per share
Balance at June 30, 1992	3,315,264	$0.25 - $2.25
Granted	–	–
Exercised	(1,113,428)	$0.25 - $2.25
Forfeited	(14,600)	$0.50
Balance at June 30, 1993	2,187,236	$0.25 - $2.25
Granted	–	–
Exercised	(727,624)	$0.25 - $2.25
Forfeited	–	–
Balance at June 30, 1994	1,459,612	$0.25 - $2.25
Granted	–	–
Exercised	(648,044)	$0.25 - $2.25
Forfeited	(20,000)	$0.50
Balance at June 30, 1995	791,568	$0.25 - $2.25

At June 30, 1995, 776,968 options were exercisable. There have been 3,160,884 options exercised under the 1987 Plan.

1992 Employee, Director and Consultant Stock Option Plan In February 1992, the Company approved and adopted an employee, director and consultant stock option plan ("the 1992 Plan"). The 1992 Plan provides for the grant of either incentive stock options or non-qualified stock options. Incentive stock options may be granted under the 1992 Plan to employees of the Company and its affiliates. Non-qualified stock options may be granted to consultants, directors, employees or officers of the Company and its affiliates. The 1992 Plan provides for an annual grant to each non-employee director on November 1 of an option to purchase 5,000 shares of common stock at an exercise price equal to the fair market value of the common stock on such date and vesting in one year. The 1992 Plan is administered by the Compensation Committee of the Board of Directors. The total number of shares that may be issued pursuant to options granted under the 1992 Plan is 18,040,000, which includes increases of 4,000,000 shares each, approved by the Board of Directors in January and July 1995, that are subject to the approval of the stockholders of the Company at the annual stockholders meeting in October 1995. The issued options vest over one-, three-, or four-year periods and are exercisable for ten years following the date of grant.

	Number of shares	Option price per share
Balance at June 30, 1992	12,000	$3.56
Granted	3,215,400	$ 3.18 - $ 9.18
Exercised	–	–
Forfeited	(8,000)	$3.68
Balance at June 30, 1993	3,219,400	$ 3.18 - $ 9.18
Granted	1,458,600	$ 9.31 - $18.25
Exercised	(187,640)	$ 3.18 - $ 7.50
Forfeited	(107,200)	$ 3.18 - $18.00
Balance at June 30, 1994	4,383,160	$ 3.18 - $18.25
Granted	11,793,598	$13.90 - $44.00
Exercised	(431,802)	$ 3.18 - $18.25
Forfeited	(460,200)	$ 3.18 - $37.69
Balance at June 30, 1995	15,284,756	$ 3.18 - $44.00

At June 30, 1995, 1,491,674 options were exercisable. There have been 619,442 options exercised under the 1992 Plan.

At June 30, 1995, the Company had 753,947 common stock options outstanding relating to options which were assumed by the Company in connection with various business combinations. The options are exercisable at prices ranging from $0.34 to $27.54 and vest over the next four years. At June 30, 1995, 237,478 options were exercisable.

Employee Stock Purchase Plan In May 1992, the Company's Board of Directors adopted an Employee Stock Purchase Plan ("the ESPP"). Under the ESPP, employees of the Company and its subsidiaries who elect to participate are granted options to purchase common stock at a 15 percent discount from the market value of such stock. The ESPP permits an enrolled employee to make contributions by having withheld from his or her salary an amount between 1 percent and 10 percent of compensation to purchase shares of common stock. The ESPP is administered by the Compensation Committee of the Board of Directors. The total number of shares of common stock that may be issued pursuant to options granted under the ESPP is 400,000. A total of 110,885 shares of common stock have been issued under the ESPP.

12 Employee Benefit Plan

Savings Plan The Company has a savings plan ("the Savings Plan") that qualifies as a deferred salary arrangement under Section 401(k) of the Internal Revenue Code. Under the Savings Plan, participating employees may defer a portion of their pretax earnings, up to the Internal Revenue Service annual contribution limit. The Company matches 50% of each employee's contributions up to a maximum of 4% of the employee's earnings. The Company's matching contribution to the Savings Plan was approximately $358,000 and $168,000 in the years ended June 30, 1995 and 1994, respectively.

13 Subsequent Event

On August 23, 1995, the Company entered into a stock purchase agreement to purchase Ubique, Ltd, an Israeli company. The Company has agreed to pay approximately $15 million ($1.5 million in cash and $13.5 million in common stock) in the transaction, which is to be accounted for under the purchase method of accounting. Subject to the results of an in-process valuation, a substantial portion of the purchase price may be allocated to in-process research and development and charged to the Company's operations in the first quarter of fiscal 1996.

Quarterly Information (unaudited)

	Quarter Ended				
	September 30,	December 31,	March 31,	June 30,	Total
Fiscal 1995[1]					
Online service revenues	$ 50,056	$ 69,712	$ 99,814	$138,916	$358,498
Other revenues	6,880	6,683	9,290	12,939	35,792
Total revenues	56,936	76,395	109,104	151,855	394,290
Income (loss) from operations	4,623	(35,258)	233	11,108	(19,294)
Net income (loss)	1,481	(38,730)	(2,587)	6,189	(33,647)
Net income (loss) per share[2]	$ 0.04	$ (0.20)	$ (0.07)	$ 0.13	$ (0.99)
Fiscal 1994					
Online service revenues	$ 14,299	$ 20,292	$ 28,853	$ 37,549	$100,993
Other revenues	4,780	4,239	2,836	2,874	14,729
Total revenues	19,079	24,531	31,689	40,423	115,722
Income from operations	531	520	1,931	1,626	4,608
Net income	303	70	1,272	905	2,550
Net income per share[2]	$ 0.01	$ –	$ 0.03	$ 0.02	$ 0.07

[1] *Historical financial information for amounts previously reported in fiscal 1995 has been adjusted to account for pooling of interest transactions.*

[2] *The sum of per-share earnings (loss) does not equal earnings (loss) per share for the year due to equivalent share calculations which are impacted by the Company's loss in 1995 and by fluctuations in the Company's common stock market prices.*

Report of Independent Auditors

Board of Directors and Stockholders
America Online, Inc.

We have audited the accompanying consolidated balance sheets of America Online, Inc. as of June 30, 1995 and 1994, and the related consolidated statements of operations, changes in stockholders' equity and cash flows for each of the three years in the period ended June 30, 1995. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of America Online, Inc. at June 30, 1995 and 1994, and the consolidated results of their operations and their cash flows for each of the three years in the period ended June 30, 1995, in conformity with generally accepted accounting principles.

As discussed in Note 9 to the consolidated financial statements, in fiscal 1994 the Company changed its method of accounting for income taxes. As discussed in Note 2 to the consolidated financial statements, in fiscal 1995 the Company changed its method of accounting for short-term investments in certain debt and equity securities.

Ernst + Young LLP

Vienna, Virginia
August 25, 1995

Stockholder Information

Market Price of Common Stock

Based on the Nasdaq National Market daily closing price, the high and low sales prices were as shown below:

	High	Low
For the quarter ended:		
September 30, 1993	$ 15.19	$ 9.13
December 31, 1993	17.50	12.63
March 31, 1994	23.00	11.94
June 30, 1994	19.44	12.56
September 30, 1994	20.56	13.75
December 31, 1994	29.25	14.94
March 31, 1995	47.38	24.63
June 30, 1995	48.13	33.50

The Company has never declared, nor has it paid, any cash dividends on its Common Stock. The Company currently intends to retain its earnings to finance future growth and, therefore, does not anticipate paying any cash dividends on its Common Stock in the foreseeable future.

As of August 30, 1995, the approximate number of stockholders of record of Common Stock was 1,117.

Annual Meeting

The Annual Meeting of Stockholders will be held on Tuesday, October 31, 1995, at 10 a.m., at the Sheraton Premiere, 8661 Leesburg Pike, Vienna, Virginia.

Form 10-K

Copies of the Company's Annual Report on Form 10-K for the year ended June 30, 1995 (excluding the exhibits thereto) are available to beneficial owners of the Company's common stock without charge, upon request to the Secretary, America Online, Inc., 8619 Westwood Center Drive, Vienna, Virginia 22182.

Exchange Information

The Company's Common Stock is traded on the Nasdaq National Market under the symbol "AMER."

Options on the Company's stock are traded on the Chicago Board Options Exchange, the American Stock Exchange, and the Pacific Stock Exchange.

Independent Auditors

Ernst & Young LLP
Vienna, Virginia

Legal Counsel

Mintz, Levin, Cohn, Ferris, Glovsky & Popeo, P.C.
Boston, Massachusetts

Transfer Agent and Registrar

The First National Bank of Boston
P.O. Box 1865
Boston, Massachusetts 02105-1865

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Officers and Directors

Executive Officers

James V. Kimsey
Chairman of the Board of Directors

Stephen M. Case
President, Chief Executive Officer and Director

David Cole
Senior Vice President; President of AOL Enterprises

Michael M. Connors
Senior Vice President; President of AOL Technologies

John L. Davies
Senior Vice President; President of AOL International

Miles Gilburne
Senior Vice President, Corporate Development

Lennert J. Leader
Senior Vice President; Chief Financial Officer and Treasurer

Theodore Leonsis
Senior Vice President; President of AOL Services Company

Marc S. Seriff
Senior Vice President, Product Research

Janice Brandt
Vice President; Senior Vice President of AOL Services Company

Richard E. Hanlon
Vice President, Investor Relations

Ellen M. Kirsh
Vice President, General Counsel and Secretary

Matthew Korn
Vice President, Operations

Barry Schuler
Vice President; President of AOL Productions

Mark Stavish
Vice President, Human Resources and Facilities

Jean N. Villanueva
Vice President, Corporate Communications

Mark Walsh
Vice President, Enterprise Solutions

Audrey Y. Weil
Vice President; Senior Vice President of AOL Services Company

Board of Directors

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